Fiscal impact reports (FIRs) are prepared by the Legislative Finance Committee (LFC) for standing finance committees of the Legislature. LFC does not assume responsibility for the accuracy of these reports if they are used for other purposes.

FISCAL IMPACT REPORT

		LAST UPDATED	2/8/24
SPONSOR	Serrato/Hemphill	**ORIGINAL DATE**	1/31/24
SHORT TITLE	Public Finance Accountability Act	**BILL NUMBER**	House Bill 271/aHAFC
		ANALYST	Carswell

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT*
(dollars in thousands)

Agency/Program	FY24	FY25	FY26	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Multiple			Up to $1,330.0	Up to $1,330.0	Recurring	General Fund

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent analysis of this legislation.

Sources of Information

LFC Files

Agency Analysis Received From
State Auditor (OSA)
Department of Finance and Administration (DFA)
Higher Education Department (HED)
Department of Agriculture (NMDA)

SUMMARY

Synopsis of HAFC Amendment to House Bill 271

The House Appropriations and Finance Committee amendment to House Bill 271 strikes the $1 million general fund appropriation.

Synopsis of Original House Bill 271

House Bill 271 enacts the Public Finance Accountability Act and appropriates $1 million from the general fund to the public accountability fund for the purpose of assisting capital outlay grantees in complying with the Audit Act. The public accountability fund is created by the bill.

HB271 codifies criteria related to financial management that make grantees eligible for capital outlay. The criteria require grantees to have completed an annual audit for the most recent fiscal year and for the audit to be a public record. If the audit documents material weaknesses or significant deficiencies, funds may not be released unless the grantee has remedied the weaknesses or deficiencies to the satisfaction of the state agency making the grant; the state agency has determined it can impose special grant conditions to address the issues; or the state agency has determined that another entity may serve as a fiscal agent for the grant.

Grantees not required to submit an audit shall demonstrate to the satisfaction the state agency making the grant that it has adequate accounting methods to legally expend funds; the state agency shall impose special grant conditions; or the state agency shall determine that another entity may serve as a fiscal agent.

HB271 directs the Department of Finance and Administration to require the above criteria to have been met before certifying projects to the State Board of Finance for issuance of severance tax bonds or making a grant to grantees. Additionally, DFA is to establish grant management and oversight requirements to ensure sales, leases, and licenses of capital assets comply with applicable law, to utilize grant agreements development by DFA, and to conduct field audits of capital outlay projects.

The effective date of this bill is July 1, 2024.

FISCAL IMPLICATIONS

Both the Higher Education Department and New Mexico Department of Agriculture note the requirement in Section 5(D) of the bill for state agencies to conduct field audits of capital outlay projects on a statistical or stratified basis will impose new operational expenses on agencies that administer capital outlay grants and require additional FTE. The operating budget impact estimated in this fiscal impact report assumes up to seven agencies would need 2 FTE each to conduct the field audits at a cost per FTE of up to $95 thousand, which represents the cost of a pay band 65 auditor. Seven agencies administer the majority of local and higher education capital outlay grants. However, the requirement for field audits may be able to be met in a more efficient and centralized manner.

SIGNIFICANT ISSUES

The State Auditor notes the provisions of HB271 have been implemented by agencies for over a decade under Executive Order 2013-006, which requires capital outlay grantees to be current on their audits, to have addressed deficiencies, and to comply with special conditions or use a fiscal agent when those requirements are not met. The executive order was intended to safeguard capital outlay appropriations by ensuring grantees demonstrated adequate financial management and accounting capabilities before funds were released. As of January 5, 74 projects from the 2023 session with total appropriations of $15 million were considered ready but had not submitted an audit and could not have funds released. As of July, more than 30 projects from 2022 were also on hold due to audit non-compliance.

The State Auditor (OSA) submitted the following analysis:

> OSA works, in consultation every year, with DFA and other executive agencies to use the OSA's Audit At-Risk List in holding agencies and local public bodies accountable for late audits and audits that result in modified, adverse, or disclaimed opinions. So far, the current process that HB271 formalizes has worked well in acting as a deterrent in public entities submitting late audit reports. It has also ensured capital outlay dollars are spent prudently and in accordance with state law.
>
> However, having this good financial government procedure only in exist in Executive Order instead of state law presents significant limitations. For example, should a future

> Executive repeal the Executive Order because of political pressures from non-compliant public entities the state would revert to increased untimely audits and limited safeguards for the expenditure of direct legislative capital outlay appropriations. Additionally, parties have questioned the legal authority (primarily the financial control statutes at NMSA 1978 §6-5-1 et seq.) for the Executive Order in the past arguing that existing statute may not be sufficient. To date, the Executive Order has survived legal challenges resulting in reasonable and beneficial uses of capital outlay procedures for public entities. However, leaving the policy and procedure in an Executive Order format may result in successful legal challenges to its authority in the future, as we would depend on judicial opinions on Executive authority instead of formal legislative intent that accompanies state statute. Also, this bill, if enacted, could represent the first major component necessary for much needed capital outlay reform.

The State Auditor has provided assistance to small public bodies in reaching audit compliance for years, though funding to the program has fluctuated. In FY24, the auditor received a $500 thousand special appropriation to support the program. The State Auditor reports approximately $2.4 million in capital outlay funding has been released as a result of the FY24 appropriation.

The Higher Education Department notes the following: "NMHED does not have information on the cost or type of assistance needed to support grantees in complying with the Audit Act. We do, however, review annual audits of higher education institutions. In our review, we can note that institutions who are not in compliance with the Audit Act have experienced turnover in key fiscal positions. This has caused delay in reconciliation and financial statement preparation, resulting in late audit submission. No information is included in the legislation requiring the Office of the State Auditor to develop eligibility criteria, application process, and award process and timelines for grantees to request funding."

PERFORMANCE IMPLICATIONS

The State Auditor states: "HB271 is one of two policy levers the OSA has to require timely compliance with financial audits and the Audit Act (the other being NMSA 1978 §12-6-3 F. that has never been operationalized where OSA reports to PED, LFC and DFA untimely audits and other sections of statute require DFA or PED to withhold operating funds from the non-compliant entity). Without this policy in place, OSA would be significantly limited in its ability to enforce timely completion of audits and would need to lean more heavily on the Executive to withhold Operating funds to reach compliance – an action that no Executive has taken to date."

ADMINISTRATIVE IMPLICATIONS

According to the State Auditor, the administrative implications of HB271 to the office are minimal since it codifies requirements that have already been implemented.

CC/rl/ne/al