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

**ORIGINAL DATE** 10/22/09
**SPONSOR** Trujillo **LAST UPDATED** 10/23/09 **HB** 28

**SHORT TITLE** Reimbursement of General Fund Capital Outlay Allotments **SB**

**ANALYST** White/Patel

## APPROPRIATION (dollars in thousands)

| Appropriation | | Recurring or Non-Rec | Fund Affected |
|---|---|---|---|
| FY09 | FY10 | | |
| | $140,000.0 | Nonrecurring | Severance Tax Bonding Fund |

(Parenthesis ( ) Indicate Expenditure Decreases)

## REVENUE (dollars in thousands)

| Estimated Revenue | | | Recurring or Non-Rec | Fund Affected |
|---|---|---|---|---|
| FY09 | FY10 | FY11 | | |
| | $140,000.0 | | Nonrecurring | General Fund |

(Parenthesis ( ) Indicate Revenue Decreases)

## SOURCES OF INFORMATION
LFC Files

Relates to Senate Bill 26

## SUMMARY

Synopsis of Bill

House Bill 28 authorizes the State Board of Finance (BOF) to issue and sell a combined $140 million of short-term tax-exempt senior severance tax and supplemental severance tax bonds in FY10. The proceeds from these sales will be transferred to the general fund for use by the Department of Finance and Administration (DFA) in FY10 to “restore allotments” made from the general fund for capital outlay appropriations made in prior fiscal years.

The bill also amends the Severance Tax Bonding Act (7-27 NMSA 1978) to expressly permit the use of supplemental sponge notes for the aforementioned purposes. The current statute restricts the use of supplemental bond proceeds solely for public school capital outlay projects.

## FISCAL IMPLICATIONS

The proposed legislation restores general fund allotments from prior year general fund capital outlay projects by using approximately $98.5 million of senior severance tax bond (STB) capacity and approximately $41.5 million from supplemental severance tax bond capacity, totaling $140 million. These funds would be one-time reversions to the general fund in order to facilitate FY10 solvency.

House Bill 28 would decrease senior severance tax bonding capacity available for appropriation during the 2010 regular session to approximately $63.1 million. The bill would further decrease supplemental capital outlay available to the Public School Capital Outlay Council (PSCOC) to $100 million in FY10. Table 1 below shows detailed capacity calculations.

**Table 1:**

| LFC FORECAST OF CAPITAL OUTLAY AVAILABLE | |
|---|---|
| ***Severance Tax Bonding*** | |
| | **FY10** |
| **Senior Long-Term Issuance** | **160.0** |
| **Senior Sponge Issuance** | **139.9** |
| Senior STB Capacity - October 2009 | 299.9 |
| **Authorized Unissued** | ***(24.3)*** |
| ***Water Project Fund (Statutory 10% of STB)*** | ***(30.0)*** |
| ***Spaceport (Laws 2006 Chapter 622)*** | ***(34.0)*** |
| ***GRIP (HB10 2008 SS)*** | ***(50.0)*** |
| ***HB 28 - Expenditure Swap*** | ***(98.5)*** |
| Net Senior STB CAPACITY | 63.1 |
| **Supplemental Long-Term Issuance** | **100.0** |
| **Supplemental Sponge Issuance** | **41.5** |
| ***HB 28 - Expenditure Swap*** | ***(41.5)*** |
| Net Supplemental STB CAPACITY | 100.0 |

Furthermore, based upon a long-term supplemental issuance of $100 million, the use of $41.5 million of supplemental severance tax bond capacity would underfund FY10 awards from the PSCOC by $11.8 million. These awards have already been made and will now have to be moved to subsequent fiscal years. The proposed legislation would also push back approximately $30 million of additional awards which were expected to be made in FY10. This problem could possibly be avoided through the issuance of additional supplemental long-term, however such an increase would take away from future capacity.

## SIGNIFICANT ISSUES

The proposed legislation requires addressing the following accounting, legal, and financial concerns:

- From an accounting standpoint this transaction also does not meet the criteria of the prior period adjustments. The criteria requires 1) a new generally accepted accounting principles (GAAP) standard being implemented; 2) a decision to use an alternative accounting principles permitted by GAAP; 3) a decision to implement changes in application of an accounting principle (for example, changes in capitalization threshold for equipment); or 4) changes resulting from the correction of an error.

- House Bill 28 specifically states that "…to restore allotments made from the general fund for capital project general fund appropriations that were made in prior sessions…" The executive contends that this proposal is not reimbursing prior year expenditures but restoring cash balances in the general fund, hence the prior period adjustment criteria are not applicable. Restoring cash balances has the same effect as reimbursing the general fund. And reimbursing the general fund has the same effect as restoring prior year cash balances to pay prior year expenditures. DFA also indicates that it will deposit the amount in the general fund with full disclosure in notes to the financial statements.

- The proposed legislation has the potential to conflict with existing state statute by using bond proceeds to fund operational expenditures. The current severance tax bonding act, Section 7-27-27 NMSA 1978, states that severance tax bonds may only be issued to "finance specific projects authorized by the legislature." Unless the projects for which expenditures will be replaced and or reimbursed are specifically listed in the proposed legislation, this bill would most likely be in violation of existing statute. Even if the projects were to be listed explicitly in the legislation, the reimbursements would go straight to the general fund not capital project funds of the specific projects. Therefore the practical effect is that these bond proceeds will be used directly to finance operational expenditures. A more appropriate approach would be to simply swap unexpended general fund projects for STB monies as opposed to attempting to reimburse previously expended general fund monies from STB proceeds. The swap approach has precedent in the use of bond proceeds to address general fund deficits. **So far no list of reimbursable capital project allotments has been provided by the Department of Finance and Administration.**

## COMPANIONSHIP

Senate Bill 24 appropriates $29 million from the Public School Capital Outlay Fund to the New Mexico Public School Insurance Authority for the purpose of paying property insurance premiums on behalf of school districts and charter schools. House Bill 28 would decrease the amount of funds available to make these payments by approximately $41.5 million. This will compound the problem of underfunded awards for FY10.

The Department of Finance and Administration has expressed concern that there would be legal issues with the use STB proceeds for insurance related expenditures. However, State Board of Finance bond counsel has yet to review this issue.

## TECHNICAL ISSUES

The use of STB proceeds to finance operational expenditures would be in conflict with federal tax guidelines for tax-exempt bonds. The federal guidelines require bond proceeds to be used solely for capital expenditures and working capital expenditures related to "depreciable assets" in order to qualify for a federal tax-exemption. Therefore these issues would have to be sold as taxable bonds which generally carry a higher interest rate than typical tax-exempt STB's. On a one-day sponge bond this increased cost would be negligible. However, it is unclear whether or not taxable bonds would be permissible, as House Bill 28 specifically requires the issuance of these bonds to "comply with the Internal Revenue Code of 1986." Therefore there is a potential conflict within the bill.

DMW:MP/svb