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

		ORIGINAL DATE	02/03/10		
SPONSOR	Smith	**LAST UPDATED**	02/04/10	**HB**	
SHORT TITLE	Short-Term Bonds to Replace Federal Funds			**SB**	192
				ANALYST	White

APPROPRIATION (dollars in thousands)

Appropriation			Recurring or Non-Rec	Fund Affected
FY10	**FY11**	FY12		
$0.0	$100,000.0	$0.0	Nonrecurring	Senior STB Capacity
$0.0	$0.0	$0.1	Recurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY10	**FY11**	**FY12**		
$0.0	$100,000.0	$0.0	Nonrecurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Conflicts with SB 185
Relates to SB 182

SOURCES OF INFORMATION
LFC Files

Responses Received From
Department of Finance and Administration (DFA)
Taxation and Revenue Department (TRD)
Department of Transportation (NMDOT)

SUMMARY

Synopsis of Bill

Senate Bill 192 authorizes the State Board of Finance (BOF) to issue short-term, or sponge, senior severance tax bonds (STB) in FY11 for the purpose of creating the “stimulus lock box” (SLB). The proposed legislation creates the SLB as a special account within the general fund subject to appropriation by the legislature for expenditure in FY12 and beyond "for the purpose of compensating for the loss of federal funds that are no longer available for expenditure by the state."

Senate Bill 192 also includes notwithstanding language explicitly defining the purposes of such bonds as eligible projects in compliance with the Severance Tax Bonding Act.

FISCAL IMPLICATIONS

The FY11 general fund budget is expected to rely on the use of a variety of federal funds which may or may not still be available for use in subsequent fiscal years. As a contingency for the elimination of these funds by the federal government the proposed legislation would use proceeds from senior STB sponge notes to fund the SLB. The funds within the SLB would only be available for appropriation upon certification that federal funds used in the preceding fiscal year's operating budget will no longer be available. If these federal funds are available, the monies will stay in the SLB and be counted toward general fund reserves. Based upon the January STB capacity estimate, insufficient FY11 STB senior sponge capacity exists to facilitate the entire $100 million appropriation authorized in Senate Bill 192. Therefore, in order to meet the cap of $100 million in appropriations to the SLB, the use of an STB sweep maybe necessary. Without the use of a sweep, only $70.4 million could be appropriated to the SLB. The mechanics of STB sweeps are discussed in more detail in the significant issues section below.

LFC FORECAST OF CAPITAL OUTLAY AVAILABLE			
Severance Tax Bonding			
	FY10	**FY11**	**FY12**
Senior Long-Term Issuance	149.5	149.5	149.5
Senior Sponge Issuance	146.8	70.4	71.7
Senior STB Capacity - January 2010	**296.3**	**219.9**	**221.2**
Potential Sweep	n/a	32.6	n/a
Bonds Issued in December			
Spaceport (Laws 2006 Chapter 622)	*(10.0)*		
Miscellaneous Projects	*(49.6)*		
Bonds to be Issued in March			
Spaceport (Laws 2006 Chapter 622)	*(24.0)*		
GRIP (HB10 2008 SS)	*(50.0)*		
Miscellaneous Projects	*(72.8)*		
Remaining Bonds to be Issued			
Authorized Unissued	*(26.0)*		
Water Project Fund (Statutory 10% of STB)	*(29.6)*	*(22.0)*	*(22.1)*
SB 192 Proposed "Stimulus Lock Box"	-	*(100.0)*	
Net Senior STB CAPACITY	**34.3**	**130.5**	**199.1**

The table above shows that the proposed legislation, through the use of a potential sweep, would decrease FY11 net senior STB capacity by up to $100 million. This would leave the legislature, with the use of a potential sweep, approximately $130.5 million to appropriate for capital outlay during the 2011 regular session. Senate Bill 192 would have no effect upon supplemental STB capacity used for public school capital outlay.

SIGNIFICANT ISSUES

Although insufficient senior STB sponge capacity exists for the appropriations laid out in Senate Bill 192, the January capacity estimate did forecast that approximately $32.6 million in excess revenues would be available at the end of FY11. These revenues would normally flow into the severance tax permanent fund (STPF), however precedent does exist which would allow the legislature to use notwithstanding language to appropriate these monies in what is known as a "sweep" or "super-sponge." The precedent for using these funds is however, limited to appropriation for capital expenditures.

An STB sweep can occur when STB revenues increase year over year. Because statutory STB capacity is determined as a percentage of the prior year's revenues, an increasing revenue environment will typically result in a large amount of STB revenue left over to revert to the severance tax permanent fund. These extra funds normally flow into the severance tax permanent fund unless they are "swept" by the legislature for use in capital projects. This type of transaction has occurred multiple times over the past 10 years due to record oil and gas revenues. In Accordance with Senate Bill 192, instead of sweeping the money for capital projects, the legislature could choose to sweep the money into the SLB discussed above for use as reserves or for operational purposes. Sweeps are typically accomplished through the use of not withstanding language in the severance tax bonding act.

The notwithstanding language needed for sweeps is usually inserted by the legislature during the regular session in which the appropriation actually occurs. Therefore such language must be inserted by the legislature in order to meet the proposed legislation's maximum appropriation level of $100 million.

Despite the fact that the proposed issuances will not be used to finance the state's current deficit, they're proposed purpose is to address anticipated future deficits caused by a lack of federal funds and therefore should still be considered deficit financing bonds. The use of deficit financing bonds, even overnight sponge deficit financing bonds, are often viewed as exposing a structural problem within a state or municipality's operating budget associated with declining revenues and increased expenditures. The bond proposal included in Senate Bill 192 is not likely to elicit this type of reaction on its own, as it deals solely with overnight notes being used as either reserves or replacing federal funds. The precedent set by such a proposal however, has a much greater impact on the state than the one-time issuance. Many investors could interpret such a precedent as a fundamental change to the severance tax bonding program as a whole, in which capital projects are no longer its main focus. Additionally, ratings agencies could look upon the precedent as a continuing facet of the state's budget practices, through which revenues are routinely taken from long-term infrastructure projects to fund expenditure levels above and beyond those supported by statutory recurring general fund revenue sources.

Over the past few years the state enjoyed record amounts of funding for long-term infrastructure projects due to record oil and gas revenues. Based on projections from the consensus revenue group however, severance tax revenues are not expected to reach those record levels again for an extended period of time. Last year, in a letter to Legislative leadership, the BOF cited various downfalls to the State's current capital outlay program and its effects on state bond ratings. The letter also stated that capital resources to the state "are inherently scarce, and are likely to be more scarce over the next several years."

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Senate Bill 192 conflicts with Senate Bill 185 which proposes to use approximately $76.3 million in FY11 senior STB sponge capacity to avoid public employee salary decreases.

Senate Bill 192 also relates and possibly conflicts with Senate Bill 208, which temporarily alters severance tax rate. If both Senate Bill 208 and Senate Bill 192 were to be enacted, sufficient short-term STB capacity may not exist to cover the entire appropriation made in Senate Bill 192.

TECHNICAL ISSUES

Bond proposals such as Senate Bill 192, normally have 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." Senate Bill 192 attempts to address this problem by using notwithstanding language to explicitly qualify its use of bond proceeds as "a project for purposes of the Severance Tax Bonding Act." In its analysis, BOF voiced concern with this language.

State Board of Finance (BOF):

> "The Severance Tax Bonding Act provides for authorized use of bond proceeds. Operational, or indirect costs are prohibited expenditures under the Act. Board of Finance bond counsel expressed concern with this bill in that it does not couch the purpose of the issuance in terms of capital projects. A court might analyze the overt use of severance tax bonds for clear general fund operating purposes as inconsistent with the long-standing usage of that bonding program for capital purposes…
>
> The bill states that the bonds it authorizes shall be deemed to be a project for the purposes of the Severance Tax Bonding Act. BOF voices concern that simply stating that compensating for the loss of federal funds that are no longer available for expenditure by the state "is a project for purposes of the Severance Tax Bonding Act" does not make it so."

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

If Senate Bill 192 is not enacted, the legislature will have up to $100 million more in net senior STB capacity to appropriate to long-term infrastructure projects in the FY11 regular session. Additionally without passage of the proposed legislation the "stimulus lock box" will not exist, thus increasing the State's difficulties addressing potential decreases in federal funding after FY11.

DMW/svb