Supplemental Severance Tax Bonding Capacity

Department of Finance and Administration

Board of Finance

Public School Capital Outlay Oversight Task Force

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Overview of Severance Tax Bonding Program

Overview of Severance Tax Bond Funding of Public School Capital

Public School capital projects are funded with proceeds from Supplemental Severance Tax Bonds and Notes.

- Primary source is <u>short-term, taxable</u> Severance Tax Notes ("Sponge Bonds")
- Long-term, tax-exempt Supplemental STBs have been used when available cash is low and will not meet capital need, as certified by the PSCOC

The Board of Finance typically estimates bonding capacity annually

- Preliminary estimates are produced in August and updated in December
- Dependent on statutory limits and 10-year revenue projections
    - Statutory limits are conservative and limit debt service to the lesser of the previous year's revenues and the current year's revenue estimate, as well as limiting to only a certain percentage of revenues.
    - Revenue estimates are from the Consensus Revenue Estimating Group and the DFA Chief Economist.

Overview of Severance Tax Bond Funding of Public School Capital

Continued

The amount of bonds/notes issued is based on the lesser of statutory capacity <u>or</u> cash available.

The final amount of Supplemental Severance Tax Notes issued is determined at the time of issuance.

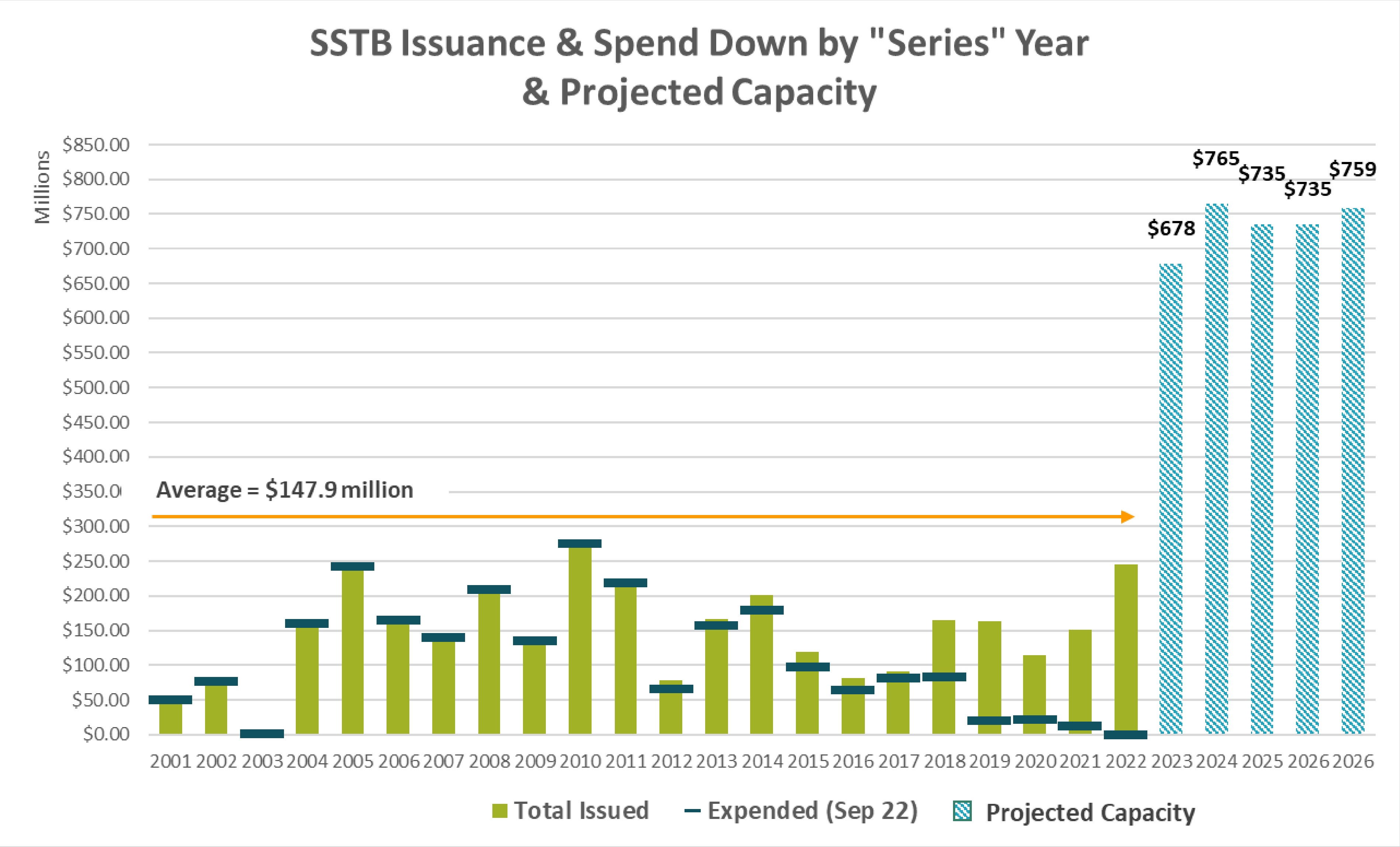
- BOF determines the amount of cash available for issuance and compares that to bonding capacity established using statutory limits.

Supplemental Severance Tax Notes are typically issued twice a year—in June and December.

Balances in the Severance Tax Bonding Fund, after notes are issued, is statutorily required to be transferred to the Severance Tax Permanent Fund.

Historical Supplemental Bond/Note Issues & Expenditures & Projected Capacity

Historical Funding, Spenddown & Projected Capacity of Supplemental Severance Tax Notes



Key Points on Historical Funding and Spenddown

Average issuance totals $147.9 million per "series" year from 2001 through 2022.

Average issuance in three highest years totals $254 million.

About 81% of funding prior to 2019 has been expended. 100% of funding expended prior to 2012.

About 8% of funding between 2020 and 2022 has been expended.

Key Points on Projected Capacity

Capacity is projected to increase by 153% between 2022 and 2023.

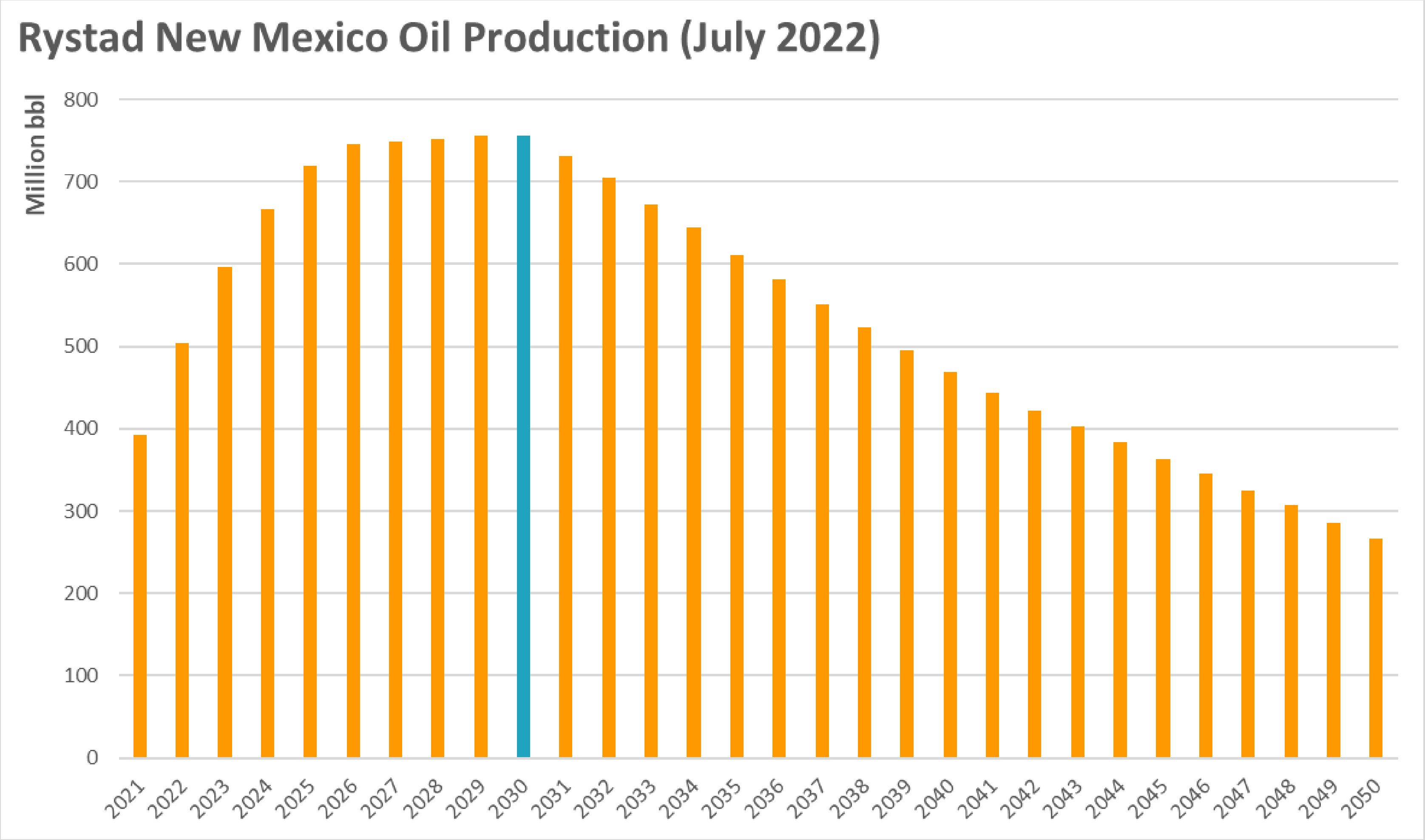
Capacity between 2023 and 2026 averages $734.5 million, 188,9% higher than the average three highest years since 2001.

Under current statutory parameters, capacity is increasing significantly as severance tax revenues increase.

What’s Driving the Increase in Bonding Capacity?

The quick answer… increased severance tax revenues from oil production.

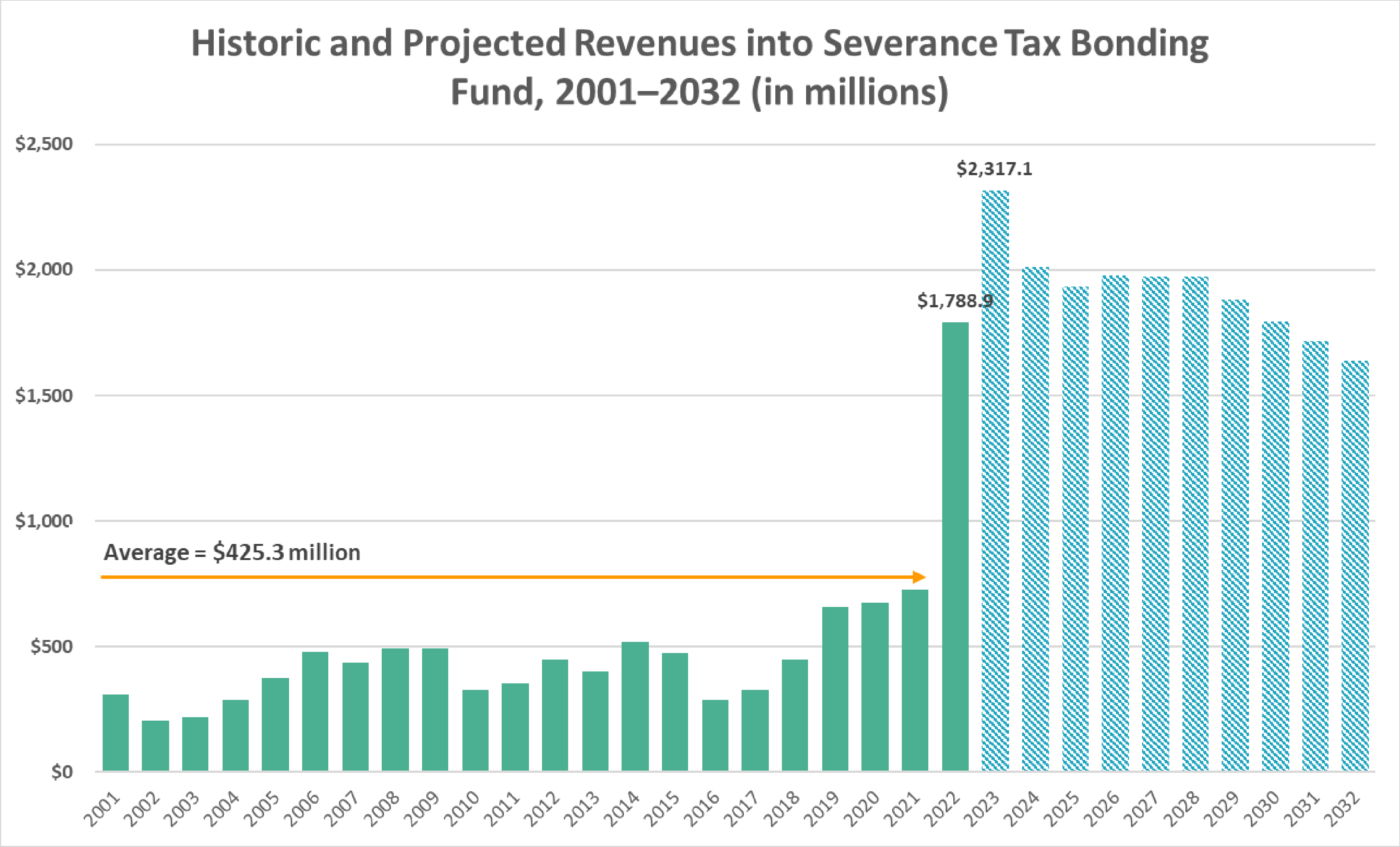
- Rystad Energy projecting peak oil production in New Mexico around 2029/2030.
- This was adjusted recently from a peak of around 2028/2029.



What’s Driving the Increase in Bonding Capacity?

High production levels + projected prices near or above $70 per barrel = significant increases in revenues to the bonding fund and resulting increases in bond and note capacity for capital projects.

Revenues are particularly high in FY 2023, and while remaining high, will begin to decline. DFA is applying declining rates to its projections slightly sooner than the Rystad peak to be somewhat conservative.



In Summary…

Oil production is driving significantly large revenue collection that is increasing capacity for Severance Tax Bond issuance.

Should the level of estimated capacity continue to be realized, large funding amounts will be available to the PSCOC for public school capital projects.

Current statute requires severance tax revenue balances to be transferred to the permanent fund twice a year. If balances are not “sponged” up for capital, those balances would be lost.

How might larger revenues, and resulting note proceeds, be utilized for public schools?

Are there larger considerations for the State’s severance tax bonding program and projected debt issuance in light of larger revenues?