Legislative Finance Committee
FINANCE FACTS
NEW MEXICO
Understanding State Financial Policy

Bonding Capacity

How much the state can spend on capital outlay projects is driven by the state's bonding capacity – its ability to repay the debt created by issuing the bonds. The state funds much of its capital outlay with severance tax bonds, repaid with severance taxes, and general obligation bonds, repaid with property taxes. Consequently, the maximum the state can bond for capital outlay projects is based on revenue projections and property values. Bonds issued for state transportation projects and projects funded by the New Mexico Finance Authority are repaid with other revenues.

General Obligation Bonds

Because general obligation bonds must be approved by voters during a general election, the Legislature considers authorizing the issuance of the bonds only during even-numbered years, those years when the state holds a statewide general election in November. General obligation bond capacity is equal to 1 percent of statewide assessed property value from the prior year less the outstanding bond debt.

Statewide assessed value is determined by the Local Government Division of the Department of Finance and Administration each fall after certification of all the county assessors' valuations. Assessed property value is equal to one-third of the actual value of all property in New Mexico, including residential, nonresidential, and oil and gas property. For example, if the total property value in New Mexico is $100 billion, the assessed value is $33.3 billion and the total bond principal outstanding cannot be more than $333 million. If outstanding principal is $10 million, the capacity is $323 million.

Because the bonds are grouped by category for consideration by voters (aging services, libraries, education, and state buildings), and voters don't always approve all the bond questions on the ballot, the value of the bonds sold can be less than the amount authorized by the Legislature.

Severance Tax Bonds

Severance tax bonds are issued against revenue from severance taxes, taxes imposed when oil, gas or other natural resource is "severed" from the ground. The revenue is deposited into the severance tax bonding fund to pay the debt service on the bonds. Money in the bond fund not needed for debt service is used for short-term notes called "sponge" bonds.Any uncommitted money in the fund is transferred twice a year to the severance tax permanent fund, which is invested by the State Investment Council.

The Board of Finance reports on severance tax bonding capacity every January 15 based on projected revenue from severance taxes. The state typically uses three types of severance-tax-backed debt: senior long-term bonds, senior notes, and supplemental notes. By law, the debt created by combination of senior long-term bonds, senior notes and supplemental notes is limited to 95 percent of the prior-year revenue.

Senior bond debt is statutorily limited to 50 percent of prior-year revenues less the debt service on outstanding senior bonds. The debt can be issued in long-term bonds, generally for 10 years, or short-term notes. Senior severance tax bond proceeds are used for capital outlay projects authorized by the Legislature. Because senior long-term bonds are repaid over 10 years, the capacity is based on estimates for 10 years of revenue and assumes the current interest rates and 10 equal long-term bond issues. Senior notes, also called "sponge bonds," are overnight issues purchased by the State Treasurer and take advantage of additional capacity remaining after the senior long-term bond issue.

Although supplemental severance tax issues can be long-term bonds or short-term notes, the state typically only issues supplemental notes to avoid the long-term obligation of bonds. Supplemental note proceeds are earmarked for public school capital outlay projects authorized by the Public School Capital Outlay Council. Supplemental notes can be issued for up to 95 percent of prior-year revenues; however, 50 percent is typically set aside for senior bonds, leaving 45 percent available. Like senior notes, supplemental notes must mature within the fiscal year.

Another bonding mechanism, called a "sweep," has also been used when revenues came in higher than projected and senior and supplemental debt did not reach 95 percent of prior-year severance tax revenue, the limit set in law.

For More Information:
- General obligation bond capacity is limited by the State Constitution, Article IX, Section 8.
- Property tax valuation methods are described in the State Constitution, Article VIII, Section 1.
- The Severance Tax Bonding Act is found in Section 7-27 NMSA 1978.
- The Board of Finance has more information about the programs and the outstanding debt for both general obligation and severance tax bonds: board.nmdfa.state.nm.us.