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

ORIGINAL DATE 2/15/15
SPONSOR Ingle **LAST UPDATED** **HB**

SHORT TITLE Reduce Severance Tax Bonding Capacity **SB** 326

ANALYST van Moorsel

APPROPRIATION (dollars in thousands)

Supplemental Severance Tax Bonding Capacity					Recurring or Nonrecurring	Fund Affected
FY15	FY16	FY17	FY18	FY19		
$0.0	$13,100.0	$16,700.0	($6,200.0)	($30,700.0)	Recurring	Public School Capital Outlay Fund

Parenthesis ( ) indicate expenditure decreases

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY15	FY16	FY17	FY18	FY19		
$0.0	$0.0	($19,800.0)	$13,100.0	$30,200.0	Recurring	STPF (transfer and earnings)
$0.0	$0.0	$0.0	$0.0	($200.0)	Recurring	General Fund

(Parenthesis ( ) indicate revenue decreases

Relates to HB 236, SB 150.

SOURCES OF INFORMATION
LFC Files

Responses Received From
Department of Finance and Administration (DFA) Board of Finance (BoF)
Public School Facilities Authority (PSFA)

SUMMARY

Synopsis of Bill

Senate Bill 326 amends the Severance Tax Bonding Act to phase in a reduction to the statutory limit for supplemental severance tax bonding capacity. Current law permits the state Board of Finance to issue short-term supplemental severance tax bonds if the debt service on such SSTBs when added to the debt service previously paid or scheduled to be paid during that fiscal year on

STBs and long term SSTBs does not exceed 95 percent of the deposits into the severance tax bonding fund during the preceding fiscal year. Considering 50 percent of the revenue is used for senior STBs, the remaining 45 percent are available for SSTBs. The bill reduces these percentages according to the following schedule:

SB 326 - Reductions in SSTB Capacity			
	Senior STB	Supplemental STB (long term)	Supplemental STB (short term)
FY15	50.0%	62.5%	95.0%
FY16	50.0%	62.5%	93.0%
FY17	50.0%	62.5%	91.0%
FY18	50.0%	62.5%	89.0%
FY19	50.0%	62.5%	87.0%
FY20	50.0%	62.5%	85.0%

The bill also changes the revenue on which supplemental STB capacity is based from "deposits into the severance tax bonding fund during the preceding fiscal year" to "the average of the deposits into the severance tax bonding fund during the current fiscal year (estimated by BoF) and deposits into the severance tax bonding fund for each of the immediately preceding four fiscal year. The effective date of this bill is July 1, 2015.

FISCAL IMPLICATIONS

The bill reduces the amount of severance tax revenue that may be used to finance supplemental severance tax bonds while increasing the amount of severance tax revenue that is transferred to the severance tax permanent fund. This has the effect of reducing estimated capital capacity as well as increasing the balance to the STPF, which in turn results in increased general fund transfers.

Current law requires bonding capacity to be estimated based on prior year severance tax revenue. As such, in years where severance taxes decrease over the previous year, more than 95 percent of current year revenue can be used to finance bonds, resulting in less than the 5 percent distribution to the STPF. For example in FY13, when $414.4 million in severance taxes were collected, only $339 not used for bonding capacity was transferred to the STPF. The provision that bases bonding capacity on a 5-year average of deposits to the bonding fund (including an estimate for the current fiscal year) may smooth out some of the volatility in the revenue.

Based on the February STB capacity estimate, the BoF estimated the impact of the reduction of supplemental bonding capacity. The BoF notes that FY16-FY17, the SSTB capacity actually increases and STPF transfers decrease because using a 5-year average of revenue adds more capacity than reducing the percentage of revenue takes away. Over 10 years, however, BoF estimates the bill will reduce SSTB capacity by a total of $197.5 million (11 percent).

The bill increases STPF transfers by a total of $225.9 million over ten years. In addition, BoF estimates that investment of this additional STPF balance at 7.5 percent compounding interest will result in an additional $37.6 million in STPF interest earnings over 10 years.

The increased corpus of the STPF, will also result in an increase in STPF distributions to the general fund, estimated to total $4.8 million over 10 years. The changes pursuant to this bill over the ten-year period of FY15-FY24 are depicted in the Board of Finance table below.

Fiscal Impact Estimate of SB326 versus Current Law

Sources of Funds (millions)	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24	10-Year
Severance Tax Bonds	-	-	-	-	-	-	-	-	-	-	-
Severance Tax Notes	-	-	-	-	-	-	-	-	-	-	-
Subtotal Senior STBs	-	-	-	-	-	-	-	-	-	-	-
Supplemental Severance Tax Bonds	-	-	-	-	-	-	-	-	-	-	-
Supplemental Severance Tax Notes	-	13.1	16.7	(6.2)	(30.7)	(40.6)	(41.9)	(35.7)	(36.6)	(35.7)	(197.5)
Subtotal Supplemental STBs	-	***13.1***	***16.7***	***(6.2)***	***(30.7)***	***(40.6)***	***(41.9)***	***(35.7)***	***(36.6)***	***(35.7)***	***(197.5)***
Total Sources of Funds	**$0.0**	**$13.1**	**$16.7**	**($6.2)**	**($30.7)**	**($40.6)**	**($41.9)**	**($35.7)**	**($36.6)**	**($35.7)**	**($197.5)**
Uses of Funds (millions)	**FY15**	**FY16**	**FY17**	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**	**FY24**	**10-Year**
Authorized but Unissued STB Projects*	-	-	-	-	-	-	-	-	-	-	-
10% Water Projects	-	-	-	-	-	-	-	-	-	-	-
Colonias Projects - 5%	-	-	-	-	-	-	-	-	-	-	-
Tribal Projects - 5%	-	-	-	-	-	-	-	-	-	-	-
New Senior STB Statewide Capital Projects	-	-	-	-	-	-	-	-	-	-	-
Education Capital	-	13.1	16.7	(6.2)	(30.7)	(40.6)	(41.9)	(35.7)	(36.6)	(35.7)	(197.5)
Total Uses of Funds	**$0.0**	**$13.1**	**$16.7**	**($6.2)**	**($30.7)**	**($40.6)**	**($41.9)**	**($35.7)**	**($36.6)**	**($35.7)**	**($197.5)**
Estimated STPF Transfer	-	-	(19.8)	14.6	30.7	40.5	30.5	35.7	37.1	56.6	225.9
STPF Earnings on Contributions - 7.5% Compounding	-	-	-	(1.5)	(0.5)	1.8	4.9	7.6	10.8	14.4	37.6
General Fund Distributions from STPF	-	-	-	-	(0.2)	(0.2)	(0.0)	0.6	1.6	3.1	4.8
Source: Department of Finance and Administration											

SIGNIFICANT ISSUES

The bill attempts to increase inflows into the severance tax permanent fund. The State Investment Council reports the STPF is in jeopardy of being permanently impaired or diminished due to the existing imbalance between contributions of state severance taxes to the STPF, and annual distributions the STPF makes to the general fund.

The following chart, provided by SIC, shows historic STPF corpus, contribution, distribution values, as well as the total amount of severance taxes collected by the state.

	Contributions to STPF	Distributions from STPF	Total Severance Taxes Collected	STPF Value
FY02	$ 32,034,751	$ 159,182,592	$ 230,506,000	3,403,010,366
FY03	$ 1,032,283	$ 170,954,868	$ 237,642,000	3,323,379,564
FY04	$ 16,318,268	$ 172,434,107	$ 305,594,000	3,632,322,981
FY05	$ 12,371,958	$ 173,249,126	$ 391,581,000	3,781,460,841
FY06	$ 123,217,261	$ 171,797,507	$ 497,336,000	4,150,806,633
FY07	$ 24,073,243	$ 170,972,506	$ 452,901,000	4,709,504,971
FY08	$ 41,413,897	$ 177,171,816	$ 511,794,000	4,314,948,773
FY09	$ 27,539,293	$ 191,292,480	$ 516,315,000	3,173,448,933
FY10	$ 3,488,067	$ 187,072,285	$ 350,123,000	3,379,772,625
FY11	$ 7,617,058	$ 184,570,731	$ 366,727,000	3,966,034,159
FY12	$ 103,888,028	$ 183,423,501	$ 462,831,000	3,880,616,288
FY13	$ 339	$ 176,172,687	$ 414,375,000	4,166,990,158
FY14	$ 129,975,882	$ 170,472,647	$ 530,668,000	4,768,257,245
FY15 (YTD@12/31)	$ 88	$ 182,722,980	$ 296,095,000	4,696,094,067

Source: State Investment Council

It should be noted that due to significant reductions in oil and gas prices since the December estimate that the February bonding capacity estimate was reduced significantly. The biggest impact from the commodity price decline was seen in the supplemental severance tax bonding capacity, which was reduced by a total of $124 million over five years, for an average reduction in annual SSTB capacity of nearly $25 million. FY16 SSTB capacity was revised downward by $54.2 million. This reduction alone will have a significant impact on the ability of the Public School Capital Outlay Council (PSCOC) to award funding for school facilities. The provisions in this bill would further reduce the availability of such funding.

According to PSFA, even under current law forecasted SSTB revenues (February, 2015) are not sufficient to maintain the average statewide Facility Condition Index (FCI). PSFA estimates that an annual state match of $157.9 million is required annually in order to maintain the FCI. Supplemental severance tax bond proceeds are not just used for public school construction, they also include SB-9 capital improvements, lease assistance, PSFA operating budget costs, and facilities master plan assistance. In its analyses of other legislation that affects the funds for public school capital outlay, PSFA has noted concern that school capital funding may fall short of the $157.9 million required to maintain the statewide FCI. PSFA has projected the impact of this bill on the FCI through FY34:

	FY16	FY17	FY18	FY19	FY20	FY25	FY30	FY34
Current Law	34.13%	34.37%	34.54%	34.71%	34.84%	35.71%	36.76%	37.72%
Maintain FCI	33.71%	33.71%	33.71%	33.71%	33.71%	33.71%	33.71%	33.71%
Proposal	34.13%	34.42%	34.66%	34.98%	35.31%	37.43%	39.74%	41.71%

PSFA notes it reported to the Public School Capital Outlay Council (PSCOC) that the current PSCOC fund balance projection shows that the rate of SSTB sales and budgeting of revenues outpace the needs of the current project schedules in the current financial plan and project delays are imminent. PSFA adds reductions in SSTB capacity available for PSCOC programs would further exacerbate the risk of project delays.

PSFA adds the current funding source for public school capital outlay was established in response to the Zuni Lawsuit. In 1999, the district court ruled that the current public school capital outlay funding system was unconstitutional and appointed a special master to review the state's progress in developing a uniform system for funding public school capital improvements and in 2002 issued a finding that the state "is in good faith and with substantial resources attempting to comply with the requirements" of the court. In 2014, Gallup McKinley County school district, one of the original litigants, requested that the court re-open the lawsuit and the request was granted. A hearing is currently scheduled in the spring of 2015. PSFA cautions that repurposing SSTB proceeds at this time may be viewed unfavorably.

TECHNICAL ISSUES

The Board of Finance identifies a technical issue with the change to using the 5-year average of revenue to the STBF to calculate bonding capacity. Per the BoF, the change appears to be intended to reduce volatility in bonding capacity and STPF contributions. BOF notes, however, that the amount of SSTB issued will always be the lesser of statutory capacity or cash on hand, adding that cash on hand will always continue to be volatile. As such, BoF questions whether the amendment will truly smooth out volatility in capacity and permanent fund transfers.

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