FISCAL IMPACT REPORT

		LAST UPDATED	2/10/2024
SPONSOR	Rodriguez	**ORIGINAL DATE**	1/31/2024
SHORT TITLE	Severance Tax Bond Fund Distributions	**BILL NUMBER**	Senate Bill 217/aSFC
		ANALYST	Carswell/Torres, Ismael

REVENUE*
(dollars in thousands)

Type	FY24	FY25	FY26	FY27	FY28	Recurring or Nonrecurring	Fund Affected
Severance Tax		$82,000.0	$82,000.0	$82,000.0	$82,000.0	Recurring	Severance Tax Permanent Fund
Investment Distributions		Positive, see fiscal implications	Positive, see fiscal implications	Positive, see fiscal implications	Positive, see fiscal implications	Recurring	General Fund

Parentheses ( ) indicate revenue decreases.
*Amounts reflect most recent analysis of this legislation.

Relates to Senate Bill 378 of the 2023 legislative session.

Sources of Information

LFC Files

Agency Analysis Received From
State Investment Council (SIC)
Board of Finance (BOF)

SUMMARY

Synopsis of SFC Amendment to Senate Bill 217

The Senate Finance Committee amendment to Senate Bill 217 makes two technical corrections, revising the savings estimate and annual distribution to $82 million and changing the final year of the distribution to 2033, consistent with the intention of the bill to make transfers for 10 years.

Synopsis of Original Senate Bill 217

Senate Bill 217 provides for $82.53 million to be distributed annually from the severance tax bonding fund to the severance tax permanent fund (STPF) unless a lesser transfer is needed for Board of Finance to avoid a potential shortfall in debt service obligations. The transfer reflects and captures the savings from the avoided debt issuance generated from using general fund for capital outlay instead of severance tax bonds. This distribution would occur on December 31st of each year from 2024 to 2034.

The bill also ensures bonding capacity for public schools is held harmless and remains at a level consistent with projections in the most recent Board of Finance estimates of severance tax bonding capacity.

This bill does not contain an effective date and, if signed, would go into effect May 15, 2024 (90 days after the Legislature adjourns).

FISCAL IMPLICATIONS

This bill directs $82 million to the severance tax permanent fund (STPF) annually from 2024 through 2034. This amount is assumed to be an estimate of the debt service that would be needed if authorized by the Legislature, and BOF issued, for the full FY24 severance tax bond (STB) capacity. Assuming this year's capital outlay bill does not include STB authorizations, this bill would direct the estimated debt service amount to the STPF instead.

If the Legislature does not authorize STBs for FY24, this bill ensures the funds would be deposited in the STPF rather than increasing supplemental severance tax bonding capacity or future capacity. The bill will not impact the distributions to the earmark funds projected in the Board of Finance's most recent estimates (water project fund, colonias infrastructure fund, tribal infrastructure fund, housing trust fund), or the bonding capacity for public school capital outlay, or future severance tax bonding capacity for new capital outlay, as projected. It is possible the limit on supplemental severance tax bonding capacity in this bill could result in an additional transfer of any remaining cash in the bonding fund to the STPF for FY24; however, staff do not have a potential estimate for this amount at this time.

The State Investment Council (SIC) estimates the bill would increase general fund distributions according to the table below:

Calendar Year	Current Estimated STPF Ending Balance ($MM)	**New Estimated STPF Ending Balance under SB217 ($MM)**
2023	$9,545.30	**$9,545.30**
2024	$9,995.30	**$10,077.90**
2025	$11,297.40	**$11,467.60**
2026	$13,223.90	**$13,486.40**
2027	$15,570.20	**$15,929.10**
2028	$18,052.30	**$18,510.80**
2029	$20,503.30	**$21,064.20**
2030	$22,988.40	**$23,653.80**
2031	$25,356.00	**$26,128.10**
2032	$27,701.70	**$28,582.50**

Fiscal Year	Current Estimated STPF Distribution to General Fund ($MM)	**New STPF Estimated Distribution to General Fund under SB217 ($MM)**	**Additional Estimated General Fund Distribution from STPF under SB217 ($MM)**
FY23	$265.80	**$265.80**	**-**
FY24	$289.60	**$289.60**	**-**
FY25	$332.80	**$332.80**	**-**
FY26	$373.80	**$374.60**	**$0.80**
FY27	$425.00	**$427.40**	**$2.40**
FY28	$486.00	**$490.90**	**$4.80**
FY29	$560.50	**$568.80**	**$8.20**
FY30	$640.50	**$653.00**	**$12.50**
FY31	$739.30	**$756.30**	**$17.00**
FY32	$849.20	**$870.90**	**$21.70**

2033	$30,043.50	**$31,035.50**
2034	$32,118.20	**$33,223.50**
2035	$34,225.70	**$35,364.00**
2036	$36,237.50	**$37,406.00**
2037	$38,164.90	**$39,361.20**
2038	$39,985.70	**$41,208.10**
2039	$41,691.90	**$42,939.50**
2040	$43,278.00	**$44,550.60**
2041	$44,739.10	**$46,036.90**
2042	$46,076.60	**$47,400.20**
2043	$47,297.10	**$48,646.80**
2044	$48,422.70	**$49,798.90**
2045	$49,545.60	**$50,949.00**
2046	$50,674.00	**$52,105.00**
2047	$51,812.50	**$53,271.70**
2048	$52,964.60	**$54,452.60**
2049	$54,132.70	**$55,649.90**
2050	$55,317.40	**$56,864.60**

FY33	$963.20	**$989.70**	**$26.50**
FY34	$1,077.30	**$1,108.60**	**$31.40**
FY35	$1,190.00	**$1,226.40**	**$36.40**
FY36	$1,299.20	**$1,340.70**	**$41.50**
FY37	$1,404.80	**$1,450.70**	**$46.00**
FY38	$1,507.10	**$1,556.70**	**$49.70**
FY39	$1,605.40	**$1,658.10**	**$52.60**
FY40	$1,698.90	**$1,753.70**	**$54.80**
FY41	$1,788.90	**$1,845.00**	**$56.10**
FY42	$1,874.00	**$1,931.40**	**$57.40**
FY43	$1,953.90	**$2,012.50**	**$58.60**
FY44	$2,028.20	**$2,088.10**	**$59.80**
FY45	$2,097.00	**$2,158.00**	**$61.00**
FY46	$2,160.20	**$2,222.50**	**$62.20**
FY47	$2,219.20	**$2,282.60**	**$63.50**
FY48	$2,275.00	**$2,339.70**	**$64.70**
FY49	$2,328.90	**$2,394.90**	**$66.00**
FY50	$2,382.10	**$2,449.40**	**$67.30**
Cumulative Additional General Fund Distribution under SB217			**$1,022.90**

While not immediate, the additional inflows into the severance tax permanent fund under this bill would increase the distributions from the STPF to the general fund. Through 2050, the estimates above show the cumulative additional distributions to the general fund could exceed $1 billion.

State Investment Office staff used the following assumptions to perform this analysis:

- For calendar years 2024-2033, we assume an expected annual compound return on STPF investments of 6.73 percent, consistent with our April 2023 asset allocation study that considers our general consultant RVK's capital market assumptions and return expectations for the various asset classes in which the STPF is invested. For calendar years 2034 and beyond, the analysis assumes the targeted rate of return of 6.75 percent.
- Contributions of severance tax revenue to the STPF under current law are assumed to be equal to the Board of Finance's estimates from December 2023, which provide inflow projections through 2033. Longer-term inflows into the fund are estimated using internal oil and gas price and production projections and applying the statutory limits for use of those revenues for bonding capacity.
- Distributions from the STPF to the general fund of 4.7 percent of the five-year average market value of the STPF, consistent with current law.

SIGNIFICANT ISSUES

Historically, severance tax revenues have been extremely volatile with transfers to the permanent fund as low as $38 (2017) in recent memory. Before the 1990s, the STPF was able to grow, due to both strong investment returns and significant inflows delivered annually from the severance tax bonding fund, with approximately 50 percent of the state's severance taxes being used for bonding, and the other half being saved for the STPF.

Starting in the late 1990s, however, the Legislature voted to reduce the distributions to the STPF in favor of more spending from the severance tax bonding fund. Ultimately, the original 50 percent of severance tax revenue distribution to the STPF was reduced to only 5 percent of the state's severance taxes being saved to the STPF, with 95 percent being spent on bonding for capital projects.

Concerns over the restructuring of these funding streams and the associated impact on the long-term viability of the STPF led lawmakers to take action in 2015, passing HB236, which adjusted the spend/save percentage of severance tax revenues from the 95/5 ratio, to a gradual implementation of a new formula that targets saving almost 14 percent (86.2 percent/13.8 percent) of the state's severance tax collections to the STPF by fiscal year 2022. The current statute allows for this percentage to continue in perpetuity, with only 13.8 percent of revenues reaching the STPF.

The following are issues noted by the State Investment Council from analysis of a similar bill in 2023:

> While there is an expectation that this change will eventually help put the STPF on stronger footing long-term, the council's fiduciary consultant RVK has noted ongoing concerns about the long-term viability of the STPF, given its historically volatile funding stream. In the 20 years from 2002-2021, the STPF received an average annual inflow from the severance tax bonding fund of less than $55 million, with contributions in some of those years totaling less than $1 million. Although the STPF received two very large contributions totaling over $1.6 billion in CY22 due to a significant rise in oil and gas prices during the year, it is likely an anomaly. The additional contributions to the STPF from Senate Bill 378 would better enable the STPF to help meet the ever-growing demands on our general fund.
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> A 2019 LFC volatility analysis found that distributions from the permanent funds are the state's most stable (i.e., least volatile) source of general fund revenue. This is because the distributions from the permanent fund are based on five-year averages of the fund's ending balance, which reduces annual volatility in the STPF caused by market swings and variance in oil and gas inflows. For example, in 2008 the value of the STPF fell nearly 32 percent during the Global Financial Crisis; however, general fund distributions from the STPF *grew* by 3.6 percent in FY08 and by 8 percent in FY09. By investing additional funds into the STPF [the bill] would further allow the permanent fund to ultimately deliver a stable and growing source of general fund revenue.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

A similar mechanism was established in 2019 (SB535) and 2023 (SB378) to set a base recurring distribution from the severance tax bonding fund to the STPF. Each year, the distribution was put in place because the annual capital outlay bill did not include senior STB authorizations and the Legislature instead directed the estimated debt service savings to the STPF.

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