State Bonding Programs

New Mexico State Board of Finance

NMHED 2021 Capital Outlay Training Series
Administration of Capital Outlay

April 6, 2023

New Mexico
Department *of* Finance
and Administration

Agenda

Municipal Bonds & Program Overview

- Municipal bonds and how they work
- New Mexico's General Obligation and Severance Tax bonding programs

Bonds as a Source of Capital Funding

- Factors and timing of bonding capacity
- Bonding capacity and capital appropriations

Selling Bonds/Notes

- Capital project review & questionnaires
- The bond sale

Bond Proceed Disbursement & Reversions

- The bond proceed draw request process
- HEI draw requirements
- Reversions

Municipal Bonds & Program Overview

Municipal bonds and how they work

New Mexico's General Obligation and Severance Tax bonding programs

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A Municipal Bond is...

A debt instrument issued by a governmental entity.

New Mexico wants to fund capital projects. To do so, it usually "borrows" the money by selling bonds.

A security.

New Mexico pledges/guarantees to pay back the money borrowed.

An obligation.

New Mexico is obligated to repay the debt

Why borrow?

Allows the state to fund capital projects regardless of the money available from the General Fund (note that General Fund dollars are not pledged to paying the debt)

Often advantageous if the interest rate on the debt is very low.

An investor buys the bonds, thus loaning money to the governmental entity (issuer).

- The governmental entity gets the money for capital projects
- The investor gets interest income on loaning that money

Debt instruments typically specify:

- **An obligation to pay**
- **A stated amount** | the principal
- **At a given time** | Known as the "term of the bond" or "maturity" and represents the borrowing period (i.e., how long does the state have to pay off the debt)
- **With interest** | Can be fixed or variable

Bonds can be taxable or tax-exempt

- Relates to whether the investor must pay taxes on income earned.

Tax-Exempt & Taxable Bonds

Tax-Exempt Bonds

- Governmental entities may issue tax-exempt bonds.
- In essence, a subsidy of the federal government because it allows interest earned on the bonds to be exempt from the bondholder's taxable income.
- Generally limited to projects that are capital assets (i.e., brick and mortar), not used by a private entity (i.e., not leased to a non-profit), and benefit the public at large.

  Why would an issuer sell a tax-exempt bond? Because it results in a lower cost of capital/borrowing because less is paid in interest.

  Why would an investor buy a tax-exempt bond? The income they receive is not taxable, the bonds serve a public purpose, and municipal bonds typically have a very low rate of default.

Taxable Bonds

- Includes all corporate bonds and some governmental bonds (issued when there's private use)

The State Board of Finance (SBOF) manages the General Obligation Bond and Severance Tax Bond programs.

General Obligation Bonds

- Issued as tax-exempt bonds every two years (usually in the spring)
- Issued with a 10-year maturity
- Secured by the full faith and credit of the State
- Paid by property tax revenues generated from the mill levy and ad valorem tax revenues on oil, gas, and minerals production and equipment
- Funds higher education, aging & long-term (senior), and library capital projects (and occasionally public education and public safety projects)
- Subject to voter approval

Overview of Bonding Programs

Severance Tax Bonds & Notes

- Long-term Senior and Supplemental Severance Tax Bonds and short-term Senior and Supplemental Severance Tax Notes are issued by the BOF.
- **Senior** Severance Tax Bonds and Notes fund capital projects appropriated by the legislature, including earmarks for tribal, colonias, and water projects.
- **Supplemental** Severance Tax Bonds and Notes are issued to fund public school capital projects, as certified and managed by PSCOC.

	SENIOR	SUPPLEMENTAL
Long-Term Bonds	Funds capital projects as authorized by the Legislature Tax-Exempt Sold 1x/year, competitively 10-year maturity	Funds public school capital projects as certified by PSCOC Tax-exempt Sold infrequently, competitively 10-year maturity
Short-Term "Sponge" Notes	Funds capital projects as authorized by the Legislature Taxable 1-2-day maturity ("pay as you go") Sold 1-2x/year (Dec/June)	Funds public school capital projects as certified by PSCOC Taxable 1-2-day maturity ("pay as you go") Sold 1-2x/year (Dec/June)

Bonds as a Source of Capital Funding

Factors and timing of bonding capacity

Bonding capacity and capital appropriations

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Determining the Size of Bonds/Notes: Key Factors in Capacity

Bonding capacity is an estimate of the amount of debt the State can incur, taking into account several key factors, including:

Statutory Limits on Debt

- GOB: 1 percent of the total assessed value of property in the State
- STB: Senior annual debt service cannot exceed 47.6 percent of the lesser of the prior year's actual severance tax revenues and the current year's estimated revenues.

  Senior and Supplemental annual debt service cannot exceed 87.8 percent of the lesser of the prior year's actual revenues and current year's estimated revenues.

Projected Future Severance Tax Revenues (primarily oil and gas)

The BOF uses 10-year severance and property tax revenue projections produced by the DFA Chief Economist and the Consensus Revenue Estimating Group (CREG).

Outstanding and future projected long-term debt service

Long-term debt service (both STBs and GOBs) is spread across a 10-year period, because the State issues its long-term bonds with a maturity of 10 years.

Determining the Size of Bonds/Notes: Capacity Timing

Bonding capacity estimates are used to guide the legislature when it makes capital project appropriations during the Legislative session.

- SBOF staff, with the State's financial adviser, prepare preliminary capacity estimates each August, upon release of new tax revenue projections from the Consensus Revenue Estimating Group (CREG) and the DFA chief economist.
- The SBOF updates capacity estimates in December for release to the legislature prior to session start in January.
- If major changes occur that will impact revenue projections during the year, SBOF staff will update the capacity estimates to reflect the most recent revenue outlook.

How Capacity is Used in Determining Capital Appropriations

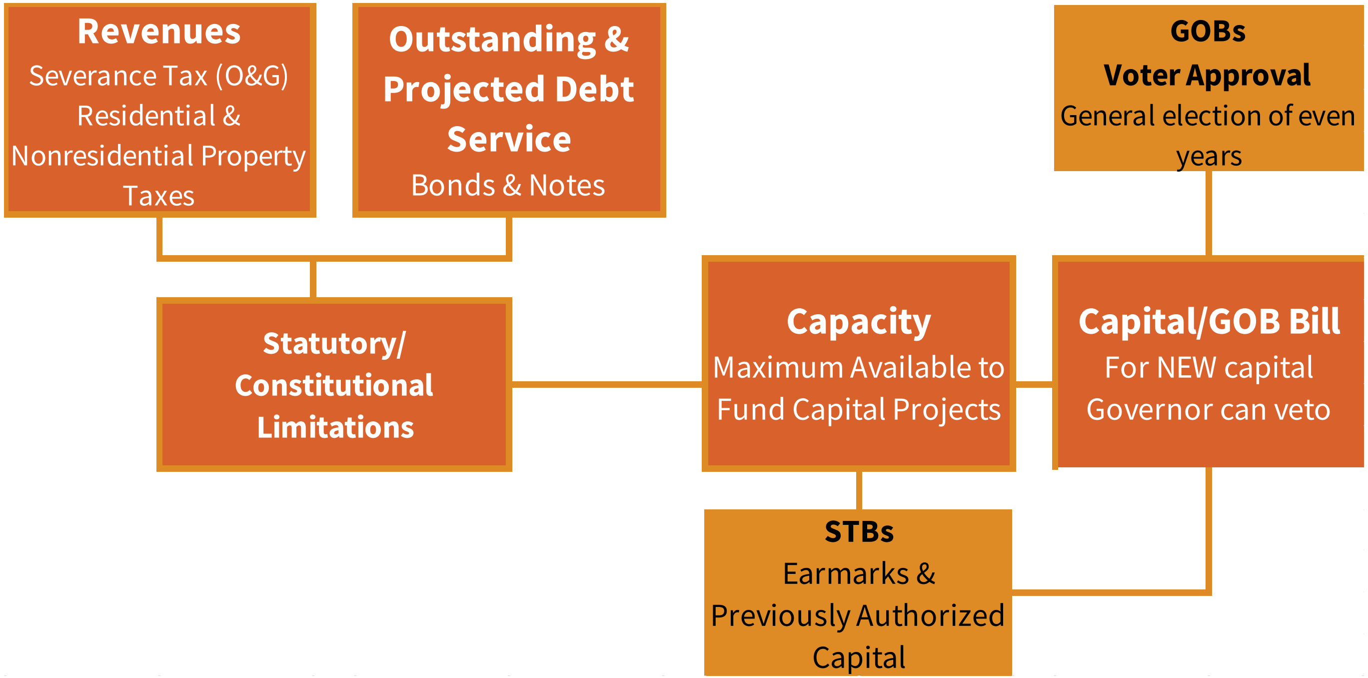
The Legislature:

- Uses capacity estimates to appropriate funding to capital outlay projects that will be funded with bond proceeds.
- Makes GOB appropriations in even years for sale in the following odd-year spring.
- Makes STB appropriations every year (typically).

The Senior Severance Tax bonding capacity available for new appropriations equals the total capacity net:

- Any past capital project appropriations not yet funded (known as "Authorized but Unissued" projects)
- Earmark projects, including water, colonias, and tribal set asides.
- Water project funding is managed by the Water Trust Board, which receives 9 percent of annual senior severance tax bonding capacity.
- Tribal project funding is managed by the Tribal Infrastructure Board, and Colonias project funding is managed by the Colonias Infrastructure Board. Each receive 4.5 percent of annual senior severance tax bonding capacity.

Capacity through Bill Signing/Voter Approval



Selling Bonds/Notes

Capital project review & questionnaires

The bond sale

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Questionnaire Process

Beginning about 3 months prior to bond sale:

Two to three rounds of review occur over ~ 2 months

- Questionnaire memo sent (Mar/Oct–STBs, Jan/Feb–GOBs)
  - Questionnare completion period ~ 2 weeks
    - Questionnaire review period ~ 2 weeks
      - Follow-up questions sent

- *Multiple rounds = multiple opportunities to finalize the questionnaires*
- *Second and third round reviews may include tax and Board counsel for projects that have special considerations*

About 2–3 weeks before bond sale:

Once questionnaire review & Q&A has been completed…

- Capital Outlay Bureau provides EO audit compliance list
  - Projects with conditions are identified
    - Board adopts resolution with final project list
      - Oversight agencies provide bond and tax certifications

Bond Sale & Closing

After the bonds sell:

- Bonds available memo is issued (~ 2 weeks)
- Conditions memo is issued (~2 to 4 weeks)
- Projects are uploaded to Bond Tracking System for use in processing draw requests
- Oversight agencies may issue grant agreements
- The capital authorized but unissued list is posted (STBs only)

Why Questionnaires are Used and Required

SBOF staff & legal counsel review all projects for compliance with:

State & Federal Tax Law

Appropriate use — planned expenditures are allowable under appropriation

Public purpose — must be for a public purpose

Project readiness — has or will begin within 6 months, full project or well-defined phase will be funded

Ability to expend funds in reasonable time — 3 years

Capital use of funds — operational uses (aka “working capital) are not allowable

Reimbursement of funds already spent — requires specific actions taken ahead of sale (strongly discouraged or not allowed)

Constitutional anti-donation concerns (when a non-public entity owns or will be managing, operating, using the capital to be funded)

Executive Order 2013–006

Requires the entity to have submitted its most recent audit prior to receiving appropriated capital funds

Questionnaire review results in a final project list and an authorized but unissued list.

Final Project list

- Projects that are determined to comply with state and federal law are "READY" and will be included in the sale.
  - Some projects are "READY" immediately upon review.
  - Projects that require additional information be provided are "FOLLOW UP" and go through Q&A to update and finalize the questionnaire information. The follow-up will result in the project being "READY" or "NOT READY".
- Projects for which remaining issues may be cleared fairly quickly but after the bond sale (primarily third-party agreements) are 'READY WITH CONDITIONS" and included in the sale but also in the conditions memo.

Authorized but Unissued List

- Projects for which the entity (1) rejects funding at that time, (2) the questionnaire is missing, or (3) state/tax law issues cannot be resolved are "NOT READY" and are added to the authorized but unissued list to be considered for a future sale.

!!! Projects have two years to be considered for a bond sale, unless statute specifies otherwise. Should a project require more time, it can be reauthorized for a time extension.

The bond sale process is very involved and typically takes 3 months in total.

Participants are broad and include several state departments, legal counsel, and the State's financial advisor, in addition to the State Board of Finance.

Bill/Voter Approval through Bond Sale

Capital Bill

Questionnaires Sent
Instructions Memo
CPMS Login

Responses Received

Questionnaire Review
SBOF Staff
Bond/Tax/Board Counsel

State Law
Appropriate Use
Readiness
Private Use

Tax Law
Capital Use
Reimbursement
Readiness

Determine Status
- Ready
- Follow Up
- Not Ready
- Anti-Donation

Further Q&A to Finalize Questionnaires

Project Lists
- Ready & Ready w/ Conditions
- Not Ready--ABU

Final Project List for Bond Sale

Held for future bond sale

Bond Proceed Disbursement

The bond proceed draw request process

HEI draw requirements

Reversions

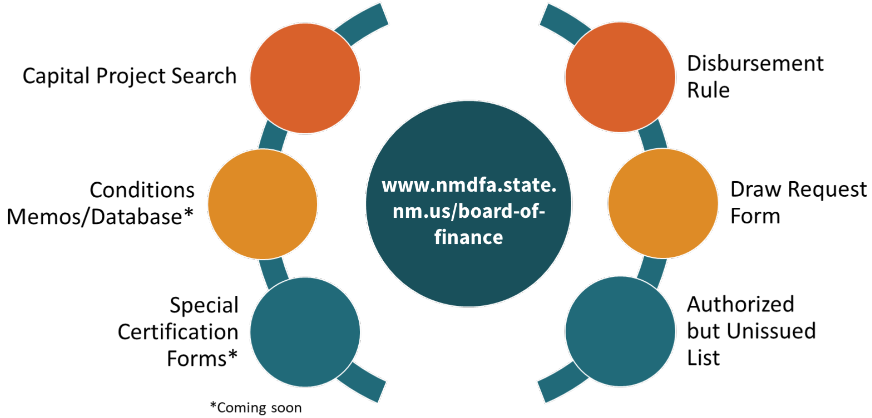
All bond proceeds are provided through the draw process on a <u>reimbursement basis</u>.

Draw request are due on the 1st & 15th of each month. Once received, SBOF:

1. Assigns draw request a document number
2. Enters request into Bond database & print Payment Voucher Backup
3. Reviews request to ensure all fiels are completed & required documents are attached
4. Payment voucher is entered into SHARE financial system
5. Payment voucher goes through multiple levels of approval at DFA
6. ACH or check is sent

When reviewing HEI draw request forms, the SBOF is looking for:

- Correct Appropriation stated in the top right corner
- Correct Bond Series filled out
- Correct Title to Appropriation
- Draw request amount stated
- Authorizing signature and Notary signature with stamp
- HED Review and Approval
- State BOF Actions (if applicable)
- Necessary back-up documentation has been provided



Draw Request Required Fields & Back-Up Documentation

Draw Request Form Required Fields

- Date, Name of HEI & Appropriation Language
- SBOF Project Number
- General Obligation, Severance Tax Bond, or Supplemental Severance Tax Bond Series
- Project Title & Appropriation Language
- Law Reference, Reversion Date & Amount of Bonds Sold
- Reauthorization Information (if applicable)
- Amount of Draw
- Accounting Information
- Authorized Signature
- Notary Public Signature and Seal

Required Back-Up Documents

- NMHED review not required
    - Project Approval Verification
    - Detailed information on expenditure timing
- NMHED Approval & SBOF and Non-SBOF review required
    - NMHED Approval Letter w/ Secretary Signature
- SBOF approval required
    - SBOF Actions/Approval
    - Evidence conditions have been satisfied (if applicable)

SBOF staff process reversions at the end of each year.

- Reversion request is sent to all oversight agencies three years after the oversight agency certifies the need of the proceeds.
  - NMHED/HEI is required to identify any proceeds that are to be reverted.
- NMHED/HEIs must have their draw requests in prior to July 8, 2023. This deadline provides adequate time to review and process requests to comply with 2.61.6 NMAC.
- If NMHED/HEI identifies draw requests after 7/8/23, they may process a manual journal entry until June 30.
- Bond proceeds revert two years (equipment) and four years (capital) following certification by the oversight agency
- If the project has encumbered obligations at the time the reversion request is sent (three years after certification), the HEI has one additional year to expend funds until reversion is required.

Thank You

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