THE STATE OF NEW MEXICO

CONTINUING DISCLOSURE

ANNUAL FINANCIAL INFORMATION FILING

FISCAL YEAR 2008

NEW MEXICO
STATE BOARD OF FINANCE

January 2009

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STATE OF NEW MEXICO
OUTSTANDING AND ADDITIONAL BONDS

Capital Program

Capital projects funded by the State of New Mexico (the "State") are financed primarily by surplus State general fund balances; General Obligation Bonds; Severance Tax Bonds, including Supplemental or Subordinate Severance Tax Bonds; and Transportation Bonds, backed primarily by the State Road Fund. Table 1 summarizes these capital funding sources for Fiscal Year 2004 through Fiscal Year 2008 and the first six months of Fiscal Year 2009 through December 31, 2008.

TABLE 1
Principal Sources of Capital Project Funding
Fiscal Year Ended June 30
(Dollars in millions)

	2004	2005	2006	2007	2008	2009 (As of 12/31/08)
Proceeds from General Obligation Bonding Program						
General Obligation Bonds	$ 0.0	$ 121.7	$ 0.0	$ 142.8	$ 0.0	$ 0.0
Subtotal	$ 0.0	$ 121.7	$ 0.0	$ 142.8	$ 0.0	$ 0.0
Proceeds from Severance Tax Bonding Program						
Severance Tax Bonds	$ 74.5	$ 87.6	$ 136.1	$ 136.4	$ 153.6	$ 0.0
Severance Tax Funding Notes[1]	63.7	87.8	102.1	193.3	150.9	169.0
Supplemental Severance Tax Bonds	10.0	10.5	0.0	0.0	0.0	0.0
Supplemental Severance Tax Funding Notes[1]	151.9	213.3	193.6	210.8	222.8	105.0
Subtotal	$ 300.0	$ 399.1	$ 431.8	$ 540.4	$ 527.3	$ 274.0
Proceeds From Other Sources						
General Fund	$ 183.4	$ 238.6	$ 454.6	$ 548.4	$ 123.0	$ 0.0
Transportation Bonds[2]	743.6	0.0	0.0	459.4	0.0	$ 100.0
Subtotal	$ 927.0	$ 238.6	$ 454.6	$ 1,007.8	$ 123.0	$ 100.0
Total	**$ 1,227.1**	**$ 759.0**	**$ 886.5**	**$ 1,690.9**	**$ 650.3**	**$ 374.0**

(1) The State Board of Finance, in order to take advantage of Bonding Fund revenue that would otherwise be transferred to the Severance Tax Permanent Fund, issues Funding Notes to the State Treasurer (which are retired within the same fiscal year with such revenue) to fund authorized projects.
(2) On May 20, 2004, the New Mexico Finance Authority issued $700,000,000 of new money bonds secured by a pledge of, and payable from, funds on deposit in the State Road Fund and the Highway Infrastructure Fund. On October 19, 2006, the New Mexico Finance Authority issued $450,400,000 of new money bonds secured by a pledge of, and payable from, funds on deposit in the State Road Fund and the Highway Infrastructure Fund. On July 1, 2008, the New Mexico Finance Authority entered into a line of credit with a bank to provide an additional $100,000,000 of available new money funding secured by a pledge of, and payable from, funds on deposit in the State Road Fund and the Highway Infrastructure Fund.
Source: New Mexico State Board of Finance.

General Obligation Bonds

Sections 7 and 8 of Article IX, of the State Constitution, limit the power of State officials to incur general obligation indebtedness extending beyond the fiscal year in the following ways:

(a) The State may borrow money not exceeding the sum of two hundred thousand dollars ($200,000) in the aggregate to meet casual deficits or failure in revenue, or for necessary expenses.

(b) Other debt may be contracted by or on behalf of the State only when authorized by law for some specified work or object. Such a law takes effect only after being submitted to the qualified electors of the State and having received a majority of all votes cast thereon at a general election. No debt may be created if the total indebtedness of the State, exclusive of the debts of the territory and several counties thereof assumed by the State, would thereby be made to exceed 1 percent of the assessed valuation of all property subject to taxation in the State, as shown by the last preceding general assessment.

(c) The State may contract debts to suppress insurrection and to provide for the public defense.

Outstanding and Additional Parity General Obligation Bonds

The principal amounts of outstanding General Obligation Bonds, as of December 31, 2008, are shown in Table 2.

TABLE 2
Outstanding General Obligation Bonds

Series	Principal Outstanding
Series 2001	$ 7,010,000
Series 2003	13,280,000
Series 2005	84,160,000
Series 2007	124,145,000
Refunding Series 2008A	71,270,000
Total	**$ 299,865,000**

Source: New Mexico State Board of Finance.

Future debt payments, by fiscal year, on General Obligation Bonds outstanding, as of December 31, 2008, are shown in Table 3.

TABLE 3
Future General Obligation Bond Debt Service[1]

Fiscal Year	Principal	Interest	Total
2009	$ 42,465,000	$ 7,710,011	$ 50,175,011
2010	42,780,000	12,870,000	55,650,000
2011	45,040,000	10,731,000	55,771,000
2012	39,325,000	8,479,000	47,804,000
2013	41,360,000	6,512,750	47,872,750
2014	27,530,000	4,444,750	31,974,750
2015	28,890,000	3,068,250	31,958,250
2016	15,840,000	1,623,750	17,463,750
2017	16,635,000	831,750	17,466,750
Total	**$299,865,000**	**$56,271,261**	**$356,136,261**

(1) Figures may not add due to rounding.
Source: New Mexico State Board of Finance.

Voters must approve the issuance of additional General Obligation Bonds, other than for refunding purposes, and the levy of additional *ad valorem* taxes. Any such additional General Obligation Bonds may be issued on a parity with, or subordinate to, all outstanding General Obligation Bonds. On November 4, 2008, the voters approved the issuance of up to $223,802,000 of additional General Obligation Bonds, which the State anticipates issuing in the first half of calendar year 2009.

Calculation of 1 Percent Bonding Limitations	
Net taxable value as of December 31, 2008	$50,463,803,991
General obligation bond limitation @ 1 percent of net taxable value	$504,638,040
Total general obligation bonds outstanding as of December 31, 2008	$299,865,000
Ratio of total debt to net taxable value	0.594%

Source: Fiscal Strategies Group.

Underlying General Obligation Bonds

The following table presents information on county, city, local and public school district debt outstanding as of June 30, 2008. The table does not include debt of special districts or community colleges.

Certain Underlying General Obligation Debt

Counties	$ 169,993,998
Cities	$ 363,068,000
Schools	$ 1,239,357,000

Source: New Mexico Department of Finance and Administration, Local Government Division and New Mexico Department of Education.

Severance Tax Bonds

The Severance Tax Bonding Act, Sections 7-27-1 to 7-27-27 NMSA 1978, as amended, permits the State Board of Finance (the "Board") to issue two categories of bonds against Severance Tax Bonding Fund (the "Bonding Fund") revenues: "New Mexico Severance Tax Bonds," referred to herein as "Senior Severance Tax Bonds," and "New Mexico Supplemental Severance Tax Bonds," referred to herein as "Supplemental Severance Tax Bonds." The Board is prohibited by statute from issuing Senior Severance Tax Bonds and short-term Senior Severance Tax Funding Notes unless the aggregate amount of total Senior Severance Tax Bonds and Funding Notes outstanding, after giving effect to the proposed issuance, can be serviced with not more than 50 percent of the annual deposits into the Bonding Fund from the preceding fiscal year. The Board is prohibited by statute from issuing Supplemental Severance Tax Bonds unless the aggregate amount of Senior Severance Tax Bonds and Supplemental Severance Tax Bonds outstanding, after giving effect to the proposed issuance, can be serviced with not more than 62.5 percent of the annual deposits into the Bonding Fund from the preceding fiscal year. In addition, short-term Supplemental Severance Tax Funding Notes may be issued if the debt service on such Supplemental Severance Tax Funding Notes, when added to the debt service previously paid or scheduled to be paid during that fiscal year on Senior and Supplemental Severance Tax Bonds and Funding Notes does not exceed 95 percent of the deposits into the Bonding Fund from the preceding fiscal year. The Senior Severance Tax Bonds and Funding Notes fund all types of capital projects while Supplemental Severance Tax Bonds and Funding Notes are earmarked for capital projects for public education.

The Board has authority to issue Supplemental Severance Tax Bonds for public school projects in amounts certified to the Board from time to time by the Public School Capital Outlay Council of the State. The lien of the pledge of such Supplemental Severance Tax Bonds (including short-term funding notes) is subordinate to any outstanding Senior Severance Tax Bonds.

Section 7-27-8 NMSA 1978 requires that on each December 31 and each June 30 the State Treasurer shall transfer to the Severance Tax Permanent Fund all money in the Bonding Fund except the amount necessary to meet all principal and interest payments on bonds payable from the Bonding Fund on the next two ensuing semiannual payment dates.

Outstanding Senior Severance Tax Bonds

The principal amounts of outstanding Senior Severance Tax Bonds, as of December 31, 2008, are shown in Table 4.

TABLE 4
Outstanding Senior Severance Tax Bonds

Severance Tax Bonds, Series 2003A	$ 41,440,000
Severance Tax Bonds, Series 2004A	45,440,000
Severance Tax Bonds, Series 2005A	64,465,000
Severance Tax Bonds, Refunding Series 2005B-1	31,130,000
Severance Tax Bonds, Series 2006A	112,950,000
Severance Tax Bonds, Series 2007A	128,635,000
Severance Tax Bonds, Series 2008A-1	149,000,000
Total	**$573,060,000**

Source: New Mexico State Board of Finance.

Future payments, by fiscal year, on outstanding Senior Severance Tax Bonds, as of December 31, 2008, are shown in Table 5.

TABLE 5
Future Senior Severance Tax Bond Debt Service[1]

Fiscal Year	Principal	Interest	Total
2009	–	$ 12,432,686	$ 12,432,686
2010	$ 70,520,000	22,972,363	93,492,363
2011	67,660,000	19,736,244	87,396,244
2012	70,955,000	16,602,913	87,557,913
2013	74,475,000	13,432,313	87,907,313
2014	69,660,000	10,425,200	80,085,200
2015	63,195,000	7,689,319	70,884,319
2016	57,165,000	5,201,350	62,366,350
2017	48,335,000	3,041,138	51,376,138
2018	33,275,000	1,378,300	34,653,300
2019	17,820,000	356,400	18,176,400
Total	**$573,060,000**	**$113,268,223**	**$686,328,223**

(1) Figures may not add due to rounding.
Source: New Mexico State Board of Finance.

Outstanding Supplemental Severance Tax Bonds

The principal amounts of Supplemental Severance Tax Bonds that are outstanding, as of December 31, 2008 are shown in Table 6.

TABLE 6
Outstanding Supplemental Severance Tax Bonds

Supplemental Severance Tax Bonds, Series 2003B	$ 5,650,000
Supplemental Severance Tax Bonds, Series 2004B	6,360,000
Supplemental Severance Tax Bonds, Series 2005B-2	21,095,000
Supplemental Severance Tax Bonds, Series 2008A-2	20,550,000
Total	**$53,655,000**

Source: New Mexico State Board of Finance.

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The future fiscal year debt payments on outstanding Supplemental Severance Tax Bonds, as of December 31, 2008, are shown in Table 7.

TABLE 7
Future Supplemental Severance Tax Bond Debt Service[(1)]

Fiscal Year	Principal	Interest	Total
2009	--	$ 1,074,210	$ 1,074,210
2010	$ 13,595,000	1,857,258	15,452,258
2011	14,145,000	1,306,746	15,451,745
2012	14,710,000	722,414	15,432,414
2013	7,700,000	288,524	7,988,524
2014	2,355,000	108,283	2,463,283
2015	1,150,000	28,750	1,178,750
Total	**$ 53,655,000**	**$ 5,386,183**	**$ 59,041,183**

(1) Figures may not add due to rounding.
Source: New Mexico State Board of Finance.

The lien of the pledge of such Supplemental Severance Tax Bonds is subordinate to any outstanding Senior Severance Tax Bonds.

Tax and Revenue Anticipation Notes

The State has issued, and expects to issue from time to time, Tax and Revenue Anticipation Notes. The Notes are not general obligations of the State. The purpose of the Notes is to fund a portion of the State's cash flow needs during the fiscal year in which the Notes are sold. As of December 31, 2008, there were not any outstanding Tax and Revenue Anticipation Notes.

Severance Tax Bonding Fund and Debt Service Requirements

Severance tax receipts contributed 89 percent of total revenue to the Bonding Fund in Fiscal Year 2008, with the remainder attributable to interest and reversions. Severance taxes are almost entirely attributable to natural gas, crude oil and coal sales. Natural gas and crude oil together accounted for approximately 96.4 percent of total Fiscal Year 2008 severance tax receipts as shown in Table 8. This percentage is calculated net of Intergovernmental Tax Credits.

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TABLE 8
Severance Tax Bonding Fund
Receipts, Disbursements and Transfers
Fiscal Year Ended June 30[1][2]
(Dollars in thousands)

	2004	2005	2006	2007	2008 (Preliminary)
Beginning Balance	$ 10,184	$ 27,175	$103,909	$240,717	$224,840
Receipts:					
Oil and Gas Severance Tax	$287,320	$372,943	$477,139	$433,357	$493,293
Other Minerals Severance Taxes	18,273	18,637	20,198	19,545	18,501
Total Severance Taxes	$305,594	$391,581	$497,336	$452,901	$511,794
Other Income:					
Interest on Investments	$ 5,475	$ 10,994	$ 27,573	$ 56,501	$ 57,410
Other financing sources	8,268	2,975	9,766	718	4,391
Subtotal	13,743	13,969	37,339	57,219	61,801
Total Receipts	$319,337	$405,549	$534,676	$510,120	$573,595
Disbursements:					
Senior Bond Debt Service	$ 67,590[3]	$ 7,551	$ 69,332	$ 72,886	$186,757
Senior Short-term Obligations[4]	63,657	87,793	102,158	74,434	269,750
Supplemental Bond Debt Service	18,215[3]	3,290	19,691	20,119	39,056
Supplemental Short-term Obligations[4]	$151,859	$213,345	$193,577	$210,830	$222,799
Fiscal Charges	618	518	738	446	665
Total Disbursements	$301,940	$312,497	$385,495	$378,715	$719,027
Transfers:					
To Severance Tax Permanent Fund	$ 406	$ 16,318	$ 12,372	$147,282	$ 404
Total transfers	$ 406	$ 16,318	$ 12,372	$147,282	$ 404
Ending Balance, June 30	$ 27,175[3]	$103,909	$240,717[5]	$224,840	$ 79,004[6]

(1) All receipts, expenditures and balances exclude amounts in rebate accounts retained for potential arbitrage rebates.
(2) Proceeds and expenditures attributable to refunding bonds are excluded from this table because such proceeds and expenditures are reserved for payments on appropriate refunding bonds and are not available for debt service payments on other Severance Tax Bonds.
(3) Includes payment of $76.37 million of debt service due July 1, 2004 on senior and supplemental bonds that was paid on June 29, 2004. Ending balance would have been $103.5 million if this payment was not made during the period.
(4) The Board, in order to take advantage of Bonding Fund revenues that would otherwise be transferred to the Severance Tax Permanent Fund, issues short-term Severance Tax funding notes and Supplemental Severance Tax funding notes to the State Treasurer which are retired within the same fiscal year with such revenue to fund authorized projects.
(5) The ending balance includes the amount of the transfer to the Severance Tax Permanent Fund, which was made on July 12, 2006 in the amount of $123.2 million and an additional transfer of $22.3 million made on December 11, 2006.
(6) The ending balance includes the amount of the transfer to the Severance Tax Permanent Fund, which was made on July 31, 2008 in the amount of $41.1 million.

Source: New Mexico State Board of Finance based on the Statewide Human Resources, Accounting, and Management Reporting System (the "SHARE System").

TABLE 9
State of New Mexico Severance Tax Bonds
Projected Receipts, Debt Service Requirements and Coverage

Fiscal Year Ending 6/30	Projected STBF Revenues	Scheduled Senior Debt Service*	Projected Senior Debt Service Coverage	Scheduled Supplemental Debt Service	Projected Supplemental Coverage
2009	$ 500,955,553	$ 96,018,973	5.22x	$ 15,390,858	4.50x
2010	448,801,847	93,492,363	4.80x	15,452,258	4.12x
2011	493,970,298	87,396,244	5.65x	15,451,745	4.80x
2012	508,648,291	87,557,913	5.81x	15,432,414	4.94x
2013	507,784,046	87,907,313	5.78x	7,988,524	5.30x
2014	499,625,616	80,085,200	6.24x	2,463,283	6.05x
2015	491,710,674	70,884,319	6.94x	1,178,750	6.82x
2016	483,795,731	62,366,350	7.76x		
2017	476,124,277	51,376,138	9.27x		
2018	468,452,822	34,653,300	13.52x		
2019	461,329,479	18,176,400	25.38x		

* Excludes debt service on refunded bonds which will be payable from escrowed securities and severance tax debt obligations sold to the State Treasurer which are retired within the same fiscal year.

Sources: New Mexico State Board of Finance and Fiscal Strategies Group.

Investments

The State Treasurer invests the funds on deposit in the Bonding Fund, including the Debt Service Account and Project Fund (established in accordance with the Bond Resolutions). The State Treasurer acts at the direction and with approval of the Board, pursuant to the State Treasurer's Investment Policy. Investments are made in securities, which are at the time legal investments of the State. No such investment or deposit shall violate any applicable restrictions imposed by the Code (defined below) or applicable Treasury Regulations relating to the market price and the existence of an established market.

Except for funds deposited into the Rebate Fund (defined in the Bond Resolutions), interest earned on the amounts on deposit in the Debt Service Account shall be retained therein, and interest earned on the amounts on deposit in the Project Fund shall be credited to the Debt Service Account and applied to the payment of principal and interest on the Bonds next becoming due. Any loss resulting from any such investment shall be charged to the applicable account from which such investments were made.

Severance Tax Collections and Reporting

Operators, purchasers and working interest owners are required to submit monthly reports to the Taxation and Revenue Department showing the total value, volume and kind of products sold from every production unit each month. Taxes must be paid at the same time and are due 55 days after the month of production. Each production report must be accompanied by a company identification number, which facilitates automated processing of return information. Production and associated tax liability is reported by "production unit" and a designation for a well or group of wells that is assigned by the Taxation and Revenue Department and is based on the master operation, property name identification and pool. A suffix is added to the production unit number to designate the specific land type and taxing authority including county, school district, and municipality.

The state maintains an automated database system ("ONGARD" for Oil and Natural Gas Administration and Revenue Database) to monitor production and sales activities of oil and natural gas producers. ONGARD functions include: managing the inventory of lands within the state and tracking all leases to determine whether royalty payments are owed to the State; monitoring all oil and gas wells for compliance with unitization agreements and other production-related information; and processing tax and royalty payments due to the State. The integrated database gives the state enhanced capabilities to compare and evaluate production, tax and royalty reports, and to issue automated exception reports.

Severance taxes received by the Taxation and Revenue Department are deposited into the Oil and Gas Suspense Fund. Using the ONGARD system, the Taxation and Revenue Department reconciles monthly information reports with the payments received to identify the appropriate amounts to distribute to each tax beneficiary. Oil and gas severance tax amounts that have been reconciled are then transferred monthly to the Bonding Fund. Table 10 presents sales volume and total sales revenue for oil and natural gas subject to severance tax.

TABLE 10
New Mexico Oil and Natural Gas Subject to Taxation
Fiscal Years Ended June 30

	2004	**2005**	**2006**	**2007**	**2008**
Oil					
Sales Volume (million barrels)	67.0	63.0	59.9	59.9	60.1
Value (millions)	$2,138.5	$2,857.8	$3,622.5	$3,541.0	$5,567.7
Average Price (per barrel)	$31.93	$45.34	$60.48	$59.11	$92.58
Natural Gas					
Sales Volume (bcf)	1,543.9	1,547.5	1,528.5	1,510.8	1,415.2
Value (millions)	$7,356.5	$9,030.2	$11,477.8	$9,900.6	$11,866.5
Average Price (per mcf)	$4.76	$5.84	$7.51	$6.55	$8.40

Source: New Mexico Taxation and Revenue Department, Tax Analysis, Research and Statistics Office (ONGARD, sales month basis as of December 2008).

Severance Taxes on Oil, Natural Gas, and Carbon Dioxide

The State collects taxes on the severance and sale of oil, natural gas and carbon dioxide. Table 11 summarizes the history of statutory tax rates imposed on natural gas, oil, and carbon dioxide. Tax rates are set by statute, Section 7-29-4 NMSA 1978, and are levied on the volume and/or value of product sold. With the exceptions noted below, tax rates have been imposed on an *ad valorem* basis, with deductions allowed for royalties paid to governments and also for certain expenses of transporting and processing products downstream of the production facility.

TABLE 11
History of Severance Tax Rates on Oil, Natural Gas and Carbon Dioxide

Year of Statutory Change	Natural Gas	Oil	Carbon Dioxide
1959	2.5%	2.5%	–
1974	3.75%	3.75%	–
1977	$0.05/mcf + surtax	$0.45/bbl + surtax	–
1980	$0.087/mcf + surtax	3.75%	–
1987	3.75%	3.75%	3.75%

Source: New Mexico Department of Finance and Administration.

Oil and Natural Gas Incentives

Although the State offers reduced severance tax rates for several categories of production, prices are above the threshold level, so none of these incentives are presently applicable. Table 12 summarizes incentive tax rates applying to various categories of production as of Fiscal Year 2008. Should prices decline in the future, some of these incentives will be applicable again.

TABLE 12
Oil and Natural Gas Tax Incentive Programs

Incentive Category	Incentive Tax Rate	Threshold Price Below Which Incentive Rate Applies	Qualified Production As a Percent of Fiscal Year 2008 Total
Restoration wells	0.0%	$24.00 per barrel(1)	0.0% Oil(3) 0.0% Natural Gas(3)
Well workover wells	2.45%	$24.00 per barrel(1)	0.0% Oil(3) 0.0% Natural Gas(3)
Stripper wells	1.875%	$1.15 per mcf-Gas(2) $15.00 per barrel-Oil(2)	0.0% Natural Gas(3) 0.0% Oil(3)
	2.8125%	$1.35 per mcf-Gas(2) $18.00 per barrel-Oil(2)	0.0% Natural Gas(3) 0.0% Oil(3)
Enhanced oil recovery	1.875%	$28.00 per barrel(1)	0.0% Oil(3)

(1) Twelve-month average price for West Texas Intermediate crude oil as reported on Oil Postings for last day of each month.
(2) Average annual taxable value of natural gas or oil sold in New Mexico during the preceding calendar year.
(3) No oil or natural gas volumes are expected to qualify for these incentives during the period because average taxable value exceeds the threshold levels.
Source: New Mexico Taxation and Revenue Department, Tax Analysis, Research and Statistics Office.

Severance Tax on Indian Land

The State can tax non-Indian oil and natural gas production on tribal land, according to United States Supreme Court precedent in *Cotton Petroleum Co. v. State of New Mexico*, 490 U.S. 163, 104 L. Ed. 2d 209, 109 S. Ct. 1968 (1989). The State's authority to impose severance taxes on Indian oil and natural gas production on tribal land was upheld by the United States District Court in New Mexico in *Jicarilla Apache Tribe v. New Mexico Taxation and Revenue Department*, No. USDC 87-922. The

Taxation and Revenue Department reports that natural gas production and crude oil production on Indian land was approximately 4.22 percent and 0.81 percent, respectively, of total taxable statewide production in 2008. The Taxation and Revenue Department estimates that oil and natural gas production on Indian land generated $13.4 million in severance tax revenues to the State in the production months corresponding to Fiscal Year 2008. The Taxation and Revenue Department estimates that coal production on Indian land ranges from 40 to 45 percent of total statewide production from year to year. No potash or copper is produced on Indian land.

Section 7-29C-1 NMSA 1978, enacted by the 1995 Legislature authorized a credit against state production and property taxes for similar taxes imposed by tribal governments. The credit applies to crude oil and natural gas from new wells drilled on or after July 1, 1995 on land within Indian reservation boundaries on March 1, 1995. The amount of the credit is 75 percent of the lesser of state taxes or tribal taxes imposed. If the applicable tribal taxes were raised after March 1, 1995, then the amount of the State's credit is lowered. The Taxation and Revenue Department estimates that total credits claimed under this provision were about $3.7 million in 2008. About $1.5 million of these credits were applied against oil and natural gas severance tax liability. The Bonding Fund revenue projection assumes that this amount will grow slowly in the future.

The 2001 Legislature enacted Sections 7-29C-2, 7-9-88.2 and 9-11-12.2 NMSA 1978, which provided a similar 75 percent intergovernmental tax credit against severance tax and severance surtax on coal mined on the Navajo Nation. The Taxation and Revenue Department reports that this credit reduced Bonding Fund revenue by $4.5 million in Fiscal Year 2008. The enactment of Section 7-31-27 NMSA 1978 created the Jicarilla Apache Tribal Capital Improvement Tax Credit, but this credit does not apply against the severance tax revenues due on the same production.

Carbon Dioxide

The Bravo Dome carbon dioxide ("CO_2") field encompasses 1.2 million acres in Harding, Union and Quay Counties in the northeastern area of the State. It contains estimated resources of 16.3 trillion cubic feet, of which 7.0 to 10.6 trillion cubic feet are considered economically recoverable. Although the state has long produced limited quantities of liquid and solid CO_2 for use in the food and the engineering industries, the main commercial value of CO_2 deposits is derived from the use of the product in its gaseous form in enhanced oil recovery projects in the Permian Basin of Texas and New Mexico. Future sales ultimately will depend on the CO_2 requirements of such projects and on the State's proportion of the market, which is shared with Colorado's Sheep Mountain and Little Sheep Mountain, McElmo Dome and Doe Creek Fields. Sales of CO_2 are expected to be approximately 101 bcf in Fiscal Year 2009 and to decline by 3 percent per year thereafter. The wellhead value of CO_2 sales was approximately $1.56 per mcf reported at the production facility in June 2008. The average price in Fiscal Year 2008 was $1.22 per mcf. An average price of $1.25 per mcf was assumed in the December 2008 revenue forecast for Fiscal Years 2009 to 2013. Severance taxes on CO_2 are levied at the rate of 3.75 percent of taxable value. Taxable value is determined by deducting royalties and the reasonable expense of trucking from the production unit to the first place of market from the value of CO_2 severed after June 30, 1990. Total deductions averaged 22.95 percent in Fiscal Year 2008.

Severance Taxes on Coal

A severance tax has been imposed on coal sales in New Mexico since 1937. Revenues were initially earmarked to the Bonding Fund in 1961. At that time the tax rate on coal was 0.125 percent. The tax rate has been changed several times over the years.

For the period July 1, 1989 through June 30, 1993, the surtax was frozen at $0.60 per ton for surface coal and $0.58 per ton for underground coal, bringing the total coal severance tax rate to $1.17 for surface coal and $1.13 for underground coal. The surtax was to begin increasing on July 1, 1993, by an amount to be determined annually by multiplying the severance tax per short ton by the percentage increase in the CPI (consumer price index) from 1991 to the calendar year just prior to the year in which the surtax rates were to be computed. However, in 1990, the surtax was eliminated on sales of coal under new contracts meeting certain criteria so that such coal will be subject to a tax of $0.55 (underground) or $0.57 (surface) per ton only. In 1992, the coal surtax exemption was expanded to include incremental sales of coal under renegotiated contracts. From 1993 to 1999, escalation of the surtax on coal was repeatedly postponed.

In 1999, the Legislature reexamined coal severance taxes in the light of deregulation of the electric power market. Increased competition in power markets makes it more difficult for utilities to pass on the cost of production taxes on coal used in generation. A 1998 study of New Mexico's coal taxes by economists at the Taxation and Revenue Department and the Department of Finance and Administration (DFA) indicated that New Mexico's taxes were among the highest in the region.[1] Based on this study, the 1999 Legislature and Governor repealed the sunset of the severance surtax exemption by Section 7-26-6.2 NMSA 1978. Coal sold and delivered pursuant to contracts dated 1990 and after are exempt from the tax. The potential cut-off of the partial exemption for contracts entered into prior to July 1, 1990 was postponed until June 30, 2009. A total of $8.9 million in severance surtax was collected in Fiscal Year 2008. The Taxation and Revenue Department calculates that collections of severance surtax have been lower by $5.9 million, $10.8 million, $12.4 million and $11.0 million in Fiscal Years 2005, 2006, 2007 and 2008, respectively, as a result of the severance surtax exemption. These estimates do not take into consideration any applicable intergovernmental tax credits.

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(1) "Taxation of Coal Production in Western States," by Kelly O'Donnell, New Mexico Taxation and Revenue Department and Dr. Thomas Clifford, New Mexico Department of Finance and Administration, presentation to the Revenue Stabilization and Tax Policy Committee, November, 1998.

TABLE 13
Coal Production, Pricing and Tax Rates
Fiscal Years 2005 to 2008[(1)]

	2005	2006	2007	2008
Total Sales Volume (Short Tons)	26,555,045	26,566,669	25,566,784	22,801,290
Surface Mined Surtax Exempt (Short Tons)	6,207,544	6,455,233	7,157,518	5,862,728
Surface Mined Non-Exempt (Short Tons)	13,434,239	13,140,540	11,412,160	11,080,122
Underground Mined Surtax Exempt (Short Tons)	6,913,261	6,970,895	6,997,106	5,858,440
Total Sales Revenue	$659,066,157	$678,600,312	$692,719,998	$654,942,711
Average Price Per Ton	$24.82	$25.54	$27.09	$28.72
Gross Severance Tax and Severance Surtax Due	$23,192,995	$24,070,557	$22,763,999	$21,743,664
Intergovernmental Tax Credit	$5,702,025	$5,886,169	$5,478,600	$4,534,144
Net Severance Tax and Severance Tax Surtax Liability	$17,490,970	$18,184,388	$17,285,399	$17,209,520
Effective Tax Rate	2.65%	2.68%	2.50%	2.63%
Effective Tax per Ton	$0.66	$0.68	$0.68	$0.75

(1) The State inaugurated the GenTax system in 2005. Therefore, Table 13 only reflects data for Fiscal Years 2005 through 2008, as Fiscal Year 2004 information is no longer comparable.
Source: New Mexico Taxation and Revenue Department, Tax Analysis, Research and Statistics Office.

Severance Taxes on Other Minerals

Many other minerals and natural resources are taxed in the State upon their severance from the earth or, in some cases, their sale or shipment. Existing tax rates are listed in Table 14. In many cases, flat percentage deductions are allowed to account for certain production costs. The result is that the taxable value is a percentage of the "full value." The "full value," in turn, is sometimes based upon published prices rather than actual prices received by the companies, as reflected in Table 14. Generally, for products with a price at the point of production, value is that price less deductions allowed for actual costs for hoisting, loading, and crushing of up to 50 percent of price. For products that must be processed before sale, deductions are allowed for cost of processing and freight charges to the point of sale. Several exceptions apply, as detailed below. For potash, the gross value is 40 percent of the posted field or market price, less those actual expenses of hoisting, crushing and loading necessary to place the severed product in marketable form and at a marketable price but allowable deductions may to exceed 50 percent. The gross value for each type of potash and potash product requiring processing or beneficiation (other than sizing) is 33.33 percent of the proceeds realized from the sale of muriate of potash and sulphate of potash magnesia, as standard grades, and 33.33 percent of the value of such products consumed in the production of other potash products, less 50 percent of such reported value as a deduction for expenses of hoisting, loading, crushing, processing, and beneficiation. Gross values for copper, lead and zinc, gold, and silver are 66.66 percent of specified Comex, London Metal Exchange cash price, London Metal Exchange Final, and London spot, U.S. Equivalent, respectively, as published in Metals Week, less 50 percent of the gross value as a deduction for the expenses of hoisting, loading, crushing, processing and beneficiation, regardless of actual expenses incurred. For molybdenum, gross value shall be the value of molybdenum contained in concentrates shipped or sold from a mine site, but in no event shall it be less than market value, less 50 percent of the sales value as a deduction for the expenses of hoisting, loading, crushing, processing and beneficiation, regardless of actual expenses incurred. For sand and gravel, in the absence of substantial evidence of a different posted field or market price, it is presumed that the gross value is $1.75 per ton. In the absence of evidence of lower deductible expenses the maximum 50 percent deduction will be allowed. In determining taxable value, rent and royalty payments to the federal government or the State government are deductible from gross value.

TABLE 14
Severance Tax Rates on Other Minerals

Mineral Resources	Tax Rate	Taxable Value as Percent of Full Value
Potash	2.500%	16.67%
Copper	0.500	16.67
Timber, Pumice, Gypsum, Clay, Fluorspar, Other	0.125	100.00
Molybdenum	0.125	50.00
Lead, Zinc	0.125	16.67
Gold	0.200	50.00
Silver	0.200	30.00
Uranium	3.500	50.00

Source: New Mexico Taxation and Revenue Department, Tax Analysis, Research and Statistics Office.

Copper prices increased significantly in Fiscal Year 2007 and continued to increase in Fiscal Year 2008, although more moderately. Prices averaged $3.52 per pound in Fiscal Year 2008, up 9.1 percent from Fiscal Year 2007's average price of $3.22 per pound. Prices for the first three months of Fiscal Year 2009 have averaged $3.44 per pound. Revenues in Fiscal Year 2008 were $760,288 up from $610,966 in 2007.

GENERAL INFORMATION CONCERNING THE STATE OF NEW MEXICO

The State was admitted as the forty-seventh state on January 6, 1912. It is the fifth largest state geographically and contains approximately 121,593 square miles.

The State's climate is characterized by sunshine and bright skies in both winter and summer. Every part of the State receives no less than 70 percent sunshine year-round. Humidity ranges from 60 percent (mornings) to 30 percent (afternoons). Evenings are crisp and cool in all seasons because of low humidity. The State has a semiarid subtropical climate with light precipitation. Thunderstorms in July and August bring most of the moisture. December to March snowfalls vary from two inches (lower Rio Grande Valley) to 300 inches (north central mountains).

Major industries in the State include oil and natural gas production, manufacturing, services, tourism, arts and crafts, agribusiness, government, and mining. Major federally-funded scientific research facilities at Los Alamos, Albuquerque and White Sands are also a notable part of the State's economy. New Mexico's farmers make a significant contribution to the economy by producing high quality agricultural products. Agriculturalists capitalize on irrigation and the State's varied climates to produce crops ranging from chile to pecans.

Governmental Organization

The Executive Branch of State government consists of a Governor, Lieutenant Governor, Secretary of State, State Auditor, State Treasurer, Attorney General, and Commissioner of Public Lands. These officials are elected to four-year terms beginning January 1 after their election. An elected

Executive Branch officer may succeed himself or herself in office once. The primary Executive Branch functions are performed by Executive Branch officeholders and their staffs, and approximately 20 cabinet departments. The Governor appoints and the Legislature confirms cabinet secretaries to lead cabinet departments. The DFA is the principal financial organization of State government and performs through its divisions the duties and functions relating to State and local government financing and general administration.

The State Board of Finance has seven voting members consisting of the Governor, the Lieutenant Governor, the State Treasurer, and four members appointed by the Governor with the advice and consent of the Senate. No more than two appointed members may be from the same political party. The Department of Finance and Administration (DFA) Secretary serves as the Executive Officer of the Board and is a non-voting Board member. The Board, in addition to other powers and duties provided by law, has general supervisory authority over the fiscal affairs of the State and over the safekeeping and depositing of all money and securities belonging to, or in the custody of, the State.

Governor Richardson serves as the President of the Board. In December 2008, President-elect Barack Obama nominated Governor Richardson to be Secretary of the United States Department of Commerce. On January 4, 2009, Governor Richardson issued a statement that he had asked the President-elect not to move forward with his nomination at that time, due to a pending investigation of a company that has done business with New Mexico State government.

The Legislature consists of 112 members and is divided into a Senate and a House of Representatives. Senators are elected for four-year terms and members of the House are elected for two-year terms. The Legislature convenes in regular session annually on the third Tuesday in January. Regular sessions are constitutionally limited in length to sixty calendar days in odd-numbered years and thirty calendar days in even-numbered years. Special sessions of the Legislature may be convened by the Governor. Extraordinary sessions may be convened by the Legislature under certain limited circumstances. Legislators do not receive any salary, but do receive per diem and mileage allowances while in session or performing official State business.

The judicial branch is composed of a statewide system including Magistrate and District Courts, the Court of Appeals and the Supreme Court. The District Courts are the trial courts of record with general jurisdiction.

Pension Funds

The Legislature enacted the Educational Retirement Act, Section 22-11-1 et seq. NMSA 1978, and the Public Employees Retirement Act, Section 10-11-1 et seq. NMSA 1978, which created the retirement plans that cover most employees of the State and its political subdivisions. These retirement plans are described below. In 1998, the voters adopted an amendment to Section 22D of Article XX of the State Constitution, which states that upon meeting the minimum service requirements of an applicable retirement plan created by law for employees of the State or any of its political subdivisions or institutions, a member of a plan shall acquire a vested property right with due process protections under the applicable provisions of the New Mexico and United States Constitutions. The Legislature establishes all financing provisions of the plans and the provisions are not subject to negotiation. Financing provisions include employee and employer contributions, fund investment provisions and benefit provisions. The balances reported below are official data as of June 30, 2008. Due to the significant market turmoil related to the downturn in the nation’s economy, New Mexico’s pension funds, along with pension funds throughout the nation, have been subject to a material loss in value for the year ended December 31, 2008.

Educational Retirement Board

The Educational Retirement Board ("ERB") had 124,872 members as of June 30, 2008, including active, retired, inactive vested and inactive non-vested members. An actuarial valuation of the Educational Retirement Fund completed by Gabriel Roeder, Smith & Co., reported that as of June 30, 2008 the actuarial value of assets was $9.3 billion and the unfunded accrued actuarial liability ("UAAL") was $3.7 billion. The funded ratio (ratio of the actuarial value of assets to actuarial accrued liability) increased from 70.5 percent at June 30, 2007 to 71.5 percent at June 30, 2008. As of June 30, 2008, the UAAL had an amortization period of 61.4 years, compared to an infinite period as of the 2007 actuarial valuation. The amortization period, also referred to as the funding period, is a calculation based on actuarial models of the period required to amortize the UAAL, assuming ERB's experience exactly follows actuarial assumptions. The actuarial assumptions include an 8 percent rate of return. As required by Governmental Standards Accounting Board ("GASB") Statement 25, the calculation is based on current contribution rates and does not take into account the statutorily scheduled increases in those rates described below. The ERB has suffered investment losses since June 30, 2008. The investment return for the quarter ended September 30, 2008 was a negative 8 percent. The investment return for the year ended September 30, 2008 was a negative 15.4 percent. The investment return for the quarter ended December 31, 2008 is estimated to be a negative 16.5 percent. The actuarial effect of losses will be reflected in future actuarial reports.

Member and employer contribution rates are established by statute. In 2005, the Legislature amended Section 22-11-21 NMSA 1978 to increase the employer contribution rate by 75 basis points (0.75 percent) for each of the seven years beginning July 1, 2005, and to increase member contribution rates by 7.5 basis points (0.075 percent) for each of the four years beginning July 1, 2005. As of July 1, 2008, the start of Fiscal Year 2009, the employer contribution rate is 11.65 percent and the member contribution rate is 7.9 percent. The member rate has reached its maximum statutory rate. The employer rate is scheduled to increase to 12.4 percent on July 1, 2009, 13.15 percent on July 1, 2010, and to its maximum statutory rate of 13.9 percent on July 1, 2011. In addition, New Mexico universities and colleges make an additional contribution of 3 percent of the salary of those employees who elect to participate in the Alternative Retirement Plan ("ARP"), a defined contribution retirement plan available to certain faculty and professional employees, to satisfy the UAAL attributable to participation in the ARP.

As indicated above, as of June 30, 2008, ERB has an amortization or funding period of 61.4 years, based on the employer and member contribution rates in effect as of July 1, 2008. The employer contribution in Fiscal Year 2009 that would have been required in order to amortize the UAAL over 30 years was 13.54 percent. Under current law, the employer rate will increase to 13.9 percent on July 1, 2011. As GASB Statement 25 does not permit the consideration of contribution rates not yet in effect, the 61.4 year funding period must be reported. In the legislative session that begins in January 2009, ERB intends to propose to increase the years of service requirement from 25 years to 30 years for new members who join the ERB on or after July 1, 2010. Existing ERB members will remain under the 25-year service requirement under the ERB proposal. The goal of the proposed legislation is to increase solvency of the Educational Retirement Fund.

Public Employees Retirement Association

Gabriel, Roeder, Smith & Co. completed an actuarial valuation of the Public Employees Retirement Association ("PERA") Fund, Judicial Retirement Fund, Magistrate Fund, Legislative Division and Volunteer Firefighter Fund ("VFF") as of June 30, 2008. The Public Employees Retirement Board accepted the actuary's conclusions that the assets, benefit values, reserves and computed contribution rates reflect utilization of an inflation rate of 4 percent per annum, compounded annually, and other risk assumption changes including salary increases for longevity and merit, the real rate of return on investments, mortality, active member withdrawals, disability and retirement rates to allow for expected future experience. For the quarter ended September 30, 2008, the quarterly PERA total fund return was a negative 11.76 percent. For the year ended September 30, 2008, the annual PERA total fund return was a negative 19.7 percent. For the quarter ended December 31, 2008, PERA estimates a total fund return of negative 15 to 20 percent.

As of June 30, 2008, PERA has an amortization or funding period of 13 years, based on the employer and member contribution rates in effect as of July 1, 2008. Member and employer rates are established pursuant to Section 10-11-1 through 10-11-141 NMSA 1978. The funded ratio (ratio of the actuarial value of assets to actuarial accrued liability) was 93 percent in Fiscal Years 2007 and 2008. PERA may consider proposing legislation to increase contributions in response to material losses in value related to the downturn in the nation's economy since June 30, 2008. Actuarial information for each fund as of June 30, 2008 is shown in Table 15.

TABLE 15
Summary of State Retirement Funds
(Dollars in thousands)

	PERA[1]	Judicial	Magistrate	VFF	Legislative
Membership	80,302	233	120	4,952	277
Actuarial Information					
Accrued Liability[2]	$ 13,740,335	$ 111,721	$ 41,721	$ 16,946	$ 21,414
Value of Assets[3]	$ 12,816,218	$ 87,430	$ 38,866	$ 48,438	$ 19,999
Unfunded (Overfunded) Accrued Liability	$ 924,117	$ 24,292	$ 2,855	($31,492)	$ 1,415
Present Value of Statutory Obligations	$ 17,351,959	$ 142,492	$ 49,378	$ 25,633	$ 23,977

(1) Includes both the state and municipal divisions.
(2) Includes the accrued liability of both the retired and active members.
(3) The valuation of assets is based on an actuarial value of assets whereby gains and losses relative to an 8 percent annual return are smoothed in over a four-year period.
Source: Public Employees Retirement Association.

New Mexico Retiree Health Care Authority

The Retiree Health Care Act was enacted in Sections 10-7C-1 through 10-7C-19 NMSA 1978, for the purpose of providing comprehensive group health insurance coverage for persons who have retired from certain public service in the State and their eligible dependents. The Retiree Health Care Act provides that the benefits offered to retired public employees may be modified, diminished or extinguished by the Legislature, and that the Act does not create any contract, trust or other rights in public employees to health care benefits.

The New Mexico Retiree Health Care Authority (the "NMRHCA"), the agency that administers the Retiree Health Care Act, has a fund base comprised of active employee payroll deductions, participating employer contributions, monthly premium contributions of enrolled participants, investment income, and amounts distributed annually from the Taxation Administration Suspense Fund ("TAA Fund"). A separate distribution from the TAA Fund, which is currently set at $3,000,000 per year, is scheduled to sunset on June 30, 2010. Employer and employee contribution rates are established in statute as is the amount distributed from the TAA Fund. Respective employer/employee contribution rates are currently 1.3 percent and 0.65 percent of the participating employee's salary. These rates combined, as well as other sources of revenue, are significantly less than what is necessary to fund the normal cost and amortization of the UAAL (as described below) over a 30-year period.

There were 42,111 NMRHCA enrolled participants as of June 30, 2008. Accrued assets at fair value on June 30, 2007 were $208,837,638 and on June 30, 2008 were estimated to be $182,166,539. For the quarter ended September 30, 2008, NMRHCA estimates losses of approximately 9 percent. For the year ended September 30, 2008, NMRHCA estimates losses of approximately 8 percent. For the quarter ended December 31, 2008, NMRHCA estimates losses of approximately 23 percent.

Based on the GASB Statement 43 valuation for Fiscal Year 2008, and assuming that the NMRHCA Fund is an equivalent arrangement to an irrevocable trust and, hence using a discount rate of 5 percent, the unfunded actuarial accrued liability ("UAAL") has been calculated to be approximately $2.9 billion. As required by GASB Statement 43, this calculation takes into consideration only current assets of the NMRHCA Fund. The UAAL is approximately $1.2 billion less than calculated in the June 30, 2006 GASB Statement 43 valuation. In addition, the June 30, 2008 GASB Statement 43 valuation indicates that the State's annual required contribution (the amount necessary to fully fund normal cost plus a 30-year amortization of the UAAL) is approximately $100 million less than in the June 30, 2006 valuation. The Board has taken several actions to reduce the UAAL in 2008 and in future years, including raising premiums and increasing contributions from retirees for the most generous plans, and continues to investigate additional opportunities including legislative initiatives to increase the combined employer/employee contribution from 1.95 percent to 3 percent over a period of three to five years.

FINANCIAL OVERVIEW

State Auditing and Accounting Systems

The financial affairs of every agency in the State are examined and audited each year by the State Auditor, personnel of the State Auditor's office designated by the State Auditor, or by the independent auditors approved by the State Auditor, as required by Section 12-6-3 NMSA 1978. The audits are conducted in accordance with generally accepted auditing standards. The audit reports include financial statements that are presented in accordance with generally accepted accounting principles.

In July 2006, the State implemented a Statewide Human Resources, Accounting and Management Reporting System (the "SHARE System"). The SHARE System replaced the State's existing Central Accounting System, central payroll system, personnel system, treasury reconciliation accounting and cashiering system, and 114 additional systems then in place at various State agencies. Since June 2007, the State has officially used SHARE as its books of record.

State Budgetary and Appropriation Process

All State agencies are required by Section 6-3-19 NMSA 1978 to submit completed budget forms to the DFA Budget Division by September 1 of each year. Guidelines and forms are provided to State agencies in advance of the September 1 deadline. Budget hearings to examine the merits of budget requests are scheduled through the fall and are usually completed by mid-December. The DFA Budget Division presents comprehensive budget recommendations to the Governor, as required by Section 6-3-15(B) NMSA 1978.

The Governor is required by Section 6-3-21 NMSA 1978 to submit a budget for the upcoming fiscal year to the Legislature in early January. The Governor's budget includes the executive recommendations for public education; higher education; State agencies; and historical information on prior expenditures, revenues and revenue projections, among other information. The State budget is contained in a General Appropriation Act, which also may contain proposals for supplemental and deficiency appropriations for the current fiscal year.

Upon passage by the Legislature, the Governor may sign the General Appropriation Act, veto it, veto line items or veto parts of it. After the Governor has signed the General Appropriation Act, the DFA Budget Division approves the agency budgets and monitors the expenditure of the funds beginning on July 1, the first day of the fiscal year.

State Treasurer's Investment Responsibilities

Pursuant to Section 6-10-10(I) NMSA 1978, the State Treasurer, with the advice and consent of the State Board of Finance, may invest money not immediately needed for government operations. These investment responsibilities are conducted in accordance with the State Treasurer's Investment Policy (the "Investment Policy"). The Investment Policy is adopted by the State Treasurer and approved by the State Board of Finance. The Investment Policy states that in keeping with the office's fiduciary responsibility, all investment decisions made by the State Treasurer will adhere to the following three fundamental principles: safety, liquidity and return. The Investment Policy governs the State Treasurer's investment activities. This policy applies to all financial assets of the State invested by the Treasurer in the exercise of the Treasurer's statutory authority or invested as directed by other agencies which have specific investment authority and for which the Treasurer acts as the investing authority. The public money includes the State's General Fund, the Local Government Investment Pool, Bond Proceeds Investment Pools, bond debt service funds, and other special funds with respect to which the State Treasurer is the investing authority.

According to the Investment Policy, an Investment Committee must be appointed by the State Treasurer with the specific purpose and responsibility of establishing, maintaining and administering the Investment Policy. The Investment Committee consists of five (5) voting members: the State Treasurer, or designee, who serves as Investment Committee Chair; the State Treasurer's Chief Investment Officer (with the State Cash Manager as an alternate); the Director of the State Board of Finance or designee; and two additional members. These additional members must be participants in the private investment community or have expert knowledge or professional experience in public finance or public fund investing. One member is appointed by the State Treasurer and approved by the Board and one member is appointed by the Board and approved by the State Treasurer.

The Investment Committee is charged with the following responsibilities:

- Reviewing the Investment Policy, no less than annually, and recommending, if advisable, modifications in the Investment Policy from time to time;
- Assessing, no less than annually, the utility and efficacy of established internal controls as loss prevention measures with respect to the investment portfolio;
- Determining, no less than annually, whether legislation affecting the investment activities of the State Treasurer should be recommended;
- Recommending investment procedures that may be useful or required in maintaining currency with public money investment practices;
- Deliberating on such topics as economic outlook, portfolio diversification and maturity structure, potential risks, the target rate of return on the investment portfolio;

- Identifying potential violations of and suggesting remedial actions to achieve conformity with the Investment Policy;
- Recommending, no less than annually, action on depositories, custodians, broker/dealers and investment managers and advisors; and
- Assessing whether the Investment Policy is being properly implemented by the individuals and entities involved in the administration and management of investment activities.

On October 26, 2005, then-New Mexico State Treasurer Robert Vigil resigned following his indictment on multiple charges of extortion, money laundering and conspiracy related to his time in office. On September 30, 2006, Mr. Vigil was convicted of one count of attempted extortion and acquitted on 23 other charges. The State Treasurer who preceded Mr. Vigil pleaded guilty to extortion for actions he took as State Treasurer.

Following the indictment of Mr. Vigil, the State engaged the law firm of Hogan and Hartson, LLP and Deloitte Financial Advisory Services L.L.P. to conduct a special audit of the State Treasurer's Office. The special audit found a significant number of internal control weaknesses and deficiencies in the operations of the State Treasurer's Office; however, the special audit did not find that the integrity of funds held at the State Treasurer's Office had been compromised. The special audit recommended a slate of legislative, rulemaking and control enhancements designed to ensure that funds held by the State Treasurer's Office are prudently invested and safely handled.

The State Treasurer's Office has implemented many of the recommendations of the special audit and has implemented a detailed corrective action plan of the type necessary to establish an effective internal control management program. Additionally, the State Treasurer's Office and the Board revised the Investment Policy to increase transparency and oversight and ensure better operating procedures in the State Treasurer's Office. These changes include a requirement to use electronic trading; a requirement to attain a financing rating for the Local Government Investment Pool from a national rating agency; a provision that the investment consultants used by the State Treasurer be approved by the Board and that they establish performance benchmarks for the State Treasurer's Office and report performance relative to that benchmark; improved reporting requirements and more meaningful controls over trading activity; requirements for the State Treasurer to adopt an employee code of conduct policy, a campaign contributions policy, and a whistleblower policy; and a requirement that the State Treasurer and employees involved in the investment process refrain from personal business activity that may impair their ability to make impartial investment decisions.

General Fund

The State derives the majority of its recurring General Fund revenue from five major sources: general and selective sales taxes, income taxes, taxes and royalties on natural resource production, investment earnings from its two permanent funds, and investments made by the State Treasurer's Office.

Weakness in crude oil and natural gas markets in the 1980s contributed to a major restructuring of the State's tax base by the 1986, 1987, 1988, 1990, 1993 and 1994 Legislatures. Reliance on sales and income taxes was increased to offset declines in mineral resource taxes and royalty revenues. In recent years, significant increases in oil and natural gas prices have resulted in an increased percentage of General Fund revenues generated from oil and gas taxes. Table 16 lists audited revenues, expenditures and ending fund balances for Fiscal Years 2005, 2006 and 2007, preliminary results for Fiscal Year 2008, and estimated results for Fiscal Year 2009.

TABLE 16
General Fund Financial Summary
Fiscal Year 2005 – Fiscal Year 2009
(Dollars in thousands)

	Actual 2005	Actual 2006	Actual 2007[4]	Preliminary 2008	Estimated 2009
A. APPROPRIATION ACCOUNT					
Recurring Receipts:					
General and Selective Sales Taxes	$ 1,946,395	$ 2,147,069	$ 2,315,105	$2,305,600	$2,387,570
Income Taxes	1,333,402	1,504,277	1,640,161	1,601,960	1,558,000
Severance Taxes	426,998	541,797	486,564	626,650	458,030
License Fees	44,265	48,971	48,959	50,690	50,400
Investment Income	547,287	590,193	602,132	623,570	646,500
Rents and Royalties	476,198	609,236	551,533	610,270	448,850
Miscellaneous Receipts	40,850	39,325	37,017	50,020	42,640
Tribal Revenue Sharing	41,263	49,520	56,158	66,560	72,000
Tobacco Settlement	38,009	34,892	0	0	0
Reversions/Adjustments	11,592	14,319	36,867	59,280	39,300
Total Recurring Receipts	**4,906,259**	**5,579,599**	**5,774,497**	**5,994,600**	**5,703,290**
Total Non-Recurring and Adjustments	**62,769**	**(62,461)**	**1**	**47,142**	**(55,700)**
Total Receipts	**4,969,028**	**5,517,138**	**5,774,498**	**6,041,742**	**5,647,590**
Recurring Appropriations:					
Legislative	15,435	16,113	17,334	18,809	20,139
Judicial	146,705	161,500	180,824	205,779	217,928
General Control	144,008	151,048	165,885	197,706	205,295
Commerce and Industry/Exam. and Lic.	48,595	47,695	51,365	58,369	61,735
Agriculture, Energy and Natural Resources	62,022	70,449	75,409	86,560	90,529
Health and Human Services	1,003,064	1,119,210	1,233,645	1,393,378	1,526,696
Public Safety	286,758	295,766	333,262	383,336	411,585
Other Education	17,950	24,705	27,805	53,982	57,053
Higher Education	670,121	714,951	761,957	846,344	884,816
Public School Support	1,974,906	2,107,196	2,265,662	2,430,696	2,551,012
Recurring Appropriations	4,369,564	4,708,633	5,113,148	5,674,958	6,026,786
Other Recurring Appropriations	15,435	0	0		
Total Recurring Appropriations	**4,384,999**	**4,708,633**	**5,113,148**	**5,674,958**	**6,026,786**
Nonrecurring Appropriations[1]:					
Capital Outlay/Supplemental/Contingency	8,924	617,522	71,057	294,879	29,262
Other Nonrecurring adj for leg	315,833	38,543	743,411		45,787
Total Nonrecurring Appropriations	**324,757**	**656,065**	**814,468**	**294,879**	**75,049**
Total Expenditures	**4,709,756**	**5,364,698**	**5,927,616**	**5,969,838**	**6,101,835**
Transfer to Appropriation Contingency Fund	0	0	0		
TRANSFER TO RESERVES	**$259,271**	**$152,440**	**$(153,119)**	$71,904	$(454,245)
B. OPERATING RESERVE					
Beginning Balance	**$ 128,780**	**$330,071**	**$359,530**	**$155,955**	**$226,359**
Revenues/Repayments/Reversions	0	0	377		
Appropriations:					
Contingencies	0	(277)	(9,300)		
Other Appropriations and Adjustments	(2,644)	(1,400)	(1,533)	(1,500)	(1,500)
Total Appropriations[2]	**(2,644)**	**(1,678)**	**(10,833)**	**(1,500)**	**(1,500)**
Transfers:					
From General Fund					
Appropriations Account	259,271	152,4	(153,119)	71,904	(454,245)
Special Session/Appropriations					
Contingency Fund			(40,000)		
To Tax Stabilization Reserve Fund	(55,336)	(121,304)			
Total Transfers	**203,935**	**31,136**	**(193,119)**	**71,904**	**(454,245)**
Ending Balance[3]	**$330,071**	**$359,530**	**$155,955**	**$226,359**	**$(229,386)**

Note: Detail may not add to column total due to independent rounding.

TABLE 16
General Fund Financial Summary
Fiscal Year 2005 – Fiscal Year 2009
(Dollars in thousands)

	Actual 2005	Actual 2006	Actual 2007[(4)]	Preliminary 2008	Estimated 2009
C. STATE SUPPORT RESERVE					
Beginning Balance	**$0**	**$0**	**$0**	**$1,000**	**$1,000**
Transfers From Operating Reserve/ Appropriation Account	0	0	1,000	0	0
Ending Balance	**$0**	**$0**	**$1,000**	**$1,000**	**$1,000**
D. APPROPRIATION CONTINGENCY FUND					
Beginning Balance, Excluding Education Reform	**$49,903**	**$42,276**	**$19,851**	**$47,664**	**$26,720**
Expenditures/Appropriations[(5)]					
Disasters	(8,113)	(13,309)	(18,161)	(17,857)	(20,000)
Other	(6,178)	(9,525)	(4,663)	0	(13,000)
Prior period adjustment for water rights (Laws 2008, Chapter 111, Section 78)			9,000	(9,000)	
Reversions	6,664	409	1,636	5,914	
Transfers From General Fund	0	0	40,000	0	0
Ending Balance, Excluding Education Reform	**42,276**	**19,851**	**47,664**	**26,720**	**(6,280)**
Education Reform					
Beginning Balance, Education Reform	**120,000**	**105,350**	**79,828**	**74,928**	**67,401**
Transfers In	0	0	0	0	0
Expenditures	(14,650)	(25,523)	(4,900)	(7,527)	
Ending Balance, Education Reform	**105,350**	**79,828**	**74,928**	**67,401**	**67,401**
Ending Balance, Appropriation Contingency Fund	**$147,626**	**$99,679**	**$122,591**	**$94,121**	**$61,121**
E. TAX STABILIZATION RESERVE					
Beginning Balance	**$77,715**	**$133,051**	**$254,355**	**$254,355**	**$254,355**
Transfers In	55,336	121,304			
Ending Balance[(6)]	**$133,051**	**$254,355**	**$254,355**	**$254,355**	**$254,355**
F. TOBACCO SETTLEMENT PERMANENT FUND RESERVE[(7)]					
Beginning Balance	**$70,688**	**$77,332**	**$84,629**	**$116,719**	**$137,851**
Transfers In	38,009	34,892	36,240	44,864	47,200
Transfers Out	(38,009)	(35,257)	(18,120)	(22,432)	(23,600)
Gains Losses	6,644	7,662	13,970	(1,300)	(30,300)
Ending Balance	**$77,332**	**$84,629**	**$116,719**	**$137,851**	**$131,151**
G. TAXPAYER DIVIDEND FUND					
Beginning Balance	**$0**	**$0**	**$0**	**$0**	**$0**
Transfers In	0	0	0	0	0
Transfers Out	0	0	0	0	0
Gains Losses	0	0	0	0	0
Ending Balance	**$0**	**$0**	**$0**	**$0**	**$0**
H. TOTAL RESERVE BALANCES					
Beginning Balance	**$447,086**	**$688,080**	**$798,193**	**$650,620**	**$713,686**
Ending Balance	**$688,080**	**$798,193**	**$650,620**	**$713,686**	**$218,241**
Reserves as a Percentage of Current Year Recurring Appropriations	15.7%	17.0%	12.7%	12.6%	3.6%

Note: Detail may not add to column total due to independent rounding

<u>NOTES TO GENERAL FUND FINANCIAL SUMMARY</u>:

Appropriation Account, Nonrecurring Appropriations:

(1) **Fiscal Year 2005 includes** $8.9 million from the General Appropriation Act of 2004; $69.813 million HB2 (Laws 2005, Chapter 33), $7.429 million SB190 (Laws 2005, Chapter 34), $238.592 million HB885 (Laws 2005, Chapter 347).

Fiscal Year 2006 includes $0.06 million from the General Appropriation Act of 2005 (Laws 2005, Chapter 33, Item 43); $0.817 million from SB 190 (Laws 2005, Chapter 34); $0.2562 from HB901 (Laws 2005, Chapter 284); $37.5 million for LIHEAP (Laws 2005 (1st SS), Chapter 2); $158.6 million from the General Appropriation Act of 2006 (Laws 2006, Chapter 109, Sections 5 and 6); $4.3 million from HB1 (Laws 2006, Chapter 1); and $454.6 million from HB622 (Laws 2006, Chapter 111).

Fiscal Year 2007 includes $68.6809 million from the General Appropriation Act of 2006 (Laws 2006, Chapter 109); and $0.2835 million from HB337 for judgeships (Laws 2006, Chapter 99, Sections 5 and 12); $2.093 million from the "Junior" bill (Laws 2006, Chapter 110); and $743.411 million from various bills from the Laws of 2007.

Fiscal Year 2008 includes $15 million water trust fund transfer from General Appropriation Act of 2007 (Laws 2007, Chapter 28); $8 million for development training programs (Laws 2007, Chapter 363), $0.188 million for judgeships (Laws 2007, Chapter 140), $12 million for faculty endowments (Laws 2007, Chapter 364), $3.2153 million for breast cancer research (Laws 2007, Chapter 26), $10.7676 million from the “Junior” bill (Laws 2007, Chapter 21), $118.3488 million from Sections 4, 5 and 6 of the General Appropriation Act of 2008 (Laws 2008, Chapter 3), $5.8982 million for expenses of the Legislature (Laws 2008, Chapter 1), and $121.4613 million for capital outlay (Laws 2008, Chapter 92).

Fiscal Year 2009 includes $18.802 million from the General Appropriation Act of 2008 (Laws 2008, Chapter 3); $0.45 million from HB140 (Laws 2008, Chapter 78); $8.4748 million from SB 165 (Laws 2008, Chapter 6); $1.535 million from SB 471 (Laws 2008, Chapter 92); and $45.7874 million from Special Session Laws 2008, Chapters 2-10.

General Fund Operating Reserve Appropriations:

(2) **Fiscal Year 2005 includes** $1.144 million for Board of Finance (“BOF”) Emergency Fund and $1.5 million contingency for corrections.

Fiscal Year 2006 includes $1.5 million for BOF Emergency Fund (Laws 2005, Chapter 33, Section 4, Subsection C); and $0.2774 million for the Corrections Department (Laws 2005, Chapter 33, Section 4, Subsection G).

Fiscal Year 2007 includes $1.533 million for BOF Emergency Fund (Laws 2006, Chapter 109), $700.0 contingency for water litigation (Laws 2002, Chapter 4(1st E.S.) as reauthorized by Laws 2006, Chapter 109); and $8.6 million contingency for the spaceport (Laws 1998 (1st SS), Chapter 13, Laws 1998 (1st SS), Chapter 11 and Laws 2005, Chapter 347, Section 173).

Fiscal Year 2008 includes $1.5 million for BOF Emergency Fund.

Fiscal Year 2009 includes $1.5 million for BOF Emergency Fund.

Year-ending Balances in the Operating Reserve:

(3) Annually, if the balance in the Operating Reserve exceeds 8 percent of the previous year's recurring appropriations, the excess over 8 percent is transferred to the Tax Stabilization Reserve.

Fiscal Year 2006 – On the date the excess over 8 percent was calculated, $8.73 million in Fiscal Year 2007 activity in the General Fund Operating Reserve had been recorded. The transfer of $121,303,940 from the Operating Reserve to the Tax Stabilization Reserve brought the balance in the Operating Reserve to 8.2 percent as of the end of Fiscal Year 2006, but to 8 percent on the date of the transfer.

State Support Reserve (See Section 22-8-31 NMSA 1978):

(4) Fiscal Year 2007 includes $1 million transfer from the Appropriation Account (Laws 2007, Chapter 28, Section 5).

Appropriation Contingency Fund Appropriations:

(5) **Fiscal Year 2005 includes** $8.113 million for disasters, $548.0 for the Secretary of State (Laws 2004, Chapter 114, Section 5, Item 28), $630.0 for the Department of Public Safety (Laws 2004, Chapter 114, Section 5, Subsection G), $5.0 million to Public Education Department (“PED”) for emergency supplemental funds to public schools (Laws 2005, Chapter 33, Section 5, Item 109). Education Reform Initiatives include $14.65 million to PED (Laws 2005, Chapter 33, Section 5 Subsection 5, Items 104, 105, 106, and 128). Includes reversions of $6.664 million for federal reimbursements for fire season 2003-2005.

Fiscal Year 2006 includes $13.309 million for disaster allotments and $0.525 million to Department of Public Safety for criminal background check contingency (Laws 2005, Chapter 33, Section 4 Subsection G). $4.5 million for Interstate Stream Commission (“ISC”) for land and water rights for augmentation; $4.5 million to ISC for augmentation services (Laws 2006, Chapter 111); and $25.522 million for Public Education Reform.

Fiscal Year 2007 includes $18.161 million for disaster allotments; $2.0 million for Department of Health (“DOH”) Behavioral Health Services Program (Laws 2006, Chapter 109); $1.9125 million for Santa Fe Community College (Laws 2006, Chapter 109); $4.9 million to PED for education reform initiatives (Laws 2007, Chapter 28); $0.750 million contingency to Corrections Department (Laws 2005, Chapter 33, Section 4) for Fiscal Year 2006; and $9 million appropriation reduction prior period adjustment for water rights appropriations (Laws 2006, Chapter 111, Sec 78 (HB 622).

Fiscal Year 2008 includes $17.9 million for disaster allotments; $9 million contingency appropriation for water rights appropriations (Laws 2006, Chapter 111, Sec 78 (HB 622; see prior period adjustment in Fiscal Year 2007); and $7.527 million for education reform appropriations from the General Appropriation Act of 2008 (Laws 2008, Chapter 3, Section 5).

Fiscal Year 2009 includes $20 million for disaster allotments; and $13 million contingency for PED (Laws 2008, Chapter 3, Section 5, Item 98).

Year-ending Balances in the Tax Stabilization Reserve:

(6) Annually, if the balance in the Tax Stabilization Reserve exceeds 6 percent of the previous year's recurring appropriations, the excess over 6 percent is transferred to the Taxpayer's Dividend Fund.

Fiscal Year 2006 – $121.3 million was transferred from the General Fund Operating Reserve, the excess in that fund of 8 percent of prior year recurring appropriations prior to the date of the transfer.

(7) **Tobacco Settlement Permanent Fund Reserve** established pursuant to Section 6-4-9 NMSA 1978.

Source: New Mexico Department of Finance and Administration.

Review of Results and Projections in the General Fund

Fiscal Year 2007. In Fiscal Year 2007, recurring General Fund revenue grew by 3.5 percent to $5.8 billion. This growth followed three consecutive years in which General Fund recurring revenue grew at least 10.0 percent year-over-year. Prices for oil and natural gas remained high by historical standards, but were lower than in Fiscal Year 2006. Mineral production tax collections fell by 10.2 percent, while rents and royalties fell 9.5 percent. General and selective sales taxes grew by 7.8 percent, while income tax growth was 9 percent. Revenues from investments increased by 2 percent. Total recurring appropriations for the fiscal year totaled $5.1 billion, representing 8.6 percent growth over the previous year. General fund balances of $814.5 million were appropriated largely for capital investments. Year-ending reserves in the General Fund decreased by $147.6 million to $650.6 million, or 12.7 percent of Fiscal Year 2007 recurring appropriations. Year-ending General Fund operating reserves did not exceed 8 percent of the 2006 Fiscal Year recurring appropriations, therefore no additional amounts were transferred from the General Fund Operating Reserve to the Tax Stabilization Reserve. The balance in the Tax Stabilization Reserve remained at $254.4 million or just under 5 percent of Fiscal Year 2007 recurring appropriations.

Fiscal Year 2008. Based upon the approved operating budget and preliminary revenue results for the 2008 Fiscal Year, recurring General Fund revenues were projected to increase by 3.8 percent to $6.0 billion. Both oil and natural gas prices peaked late in the fiscal year, with oil prices averaging $132.14 per barrel in June 2008 for New Mexico producers. Natural gas prices ranged from $6.25 per mcf in August 2007 to $11.70 per mcf in June 2008. On balance, this strength in mineral production taxes and royalties covered slow growth in the broad-based taxes. Mineral production taxes and rents and royalties increased 28.8 percent and 10.6 percent respectively. General and selective sales taxes were projected to decline for the fiscal year by 0.4 percent, while income taxes declined by 2.3 percent, largely because of the final step in the 2003 personal income tax rate cuts. Although short-term interest rates decreased in the course of the fiscal year, investment income grew by 3.6 percent. Total recurring appropriations in the budget for the fiscal year totaled $5.7 billion, representing 11.0 percent growth over the previous year. The Legislature appropriated and the Governor approved $294.9 million for nonrecurring projects during the 2008 regular legislative session. Fiscal Year 2008 year-end reserves in the General Fund are expected to increase by $63.1 million, up to $713.7 million, or 12.6 percent of Fiscal Year 2008 recurring appropriations.

Fiscal Year 2009. Based upon revenue projections for Fiscal Year 2009 made in early December 2008, recurring General Fund revenues are projected to decrease by 4.9 percent to $5.7 billion. The price of oil is expected to average $69.00 per barrel and the price of natural gas is expected to average $6.05 per mcf for the fiscal year. Results and data published since December 1, 2008 suggest that the next revenue update, scheduled for February 2009, may show additional weakness in both the mineral taxes and royalties and the broad-based taxes, attributable to the national recession which began December 2007. General and selective sales taxes are projected to grow by 0.2 percent (after adjusting for an accounting anomaly) while income taxes are projected to decrease by 2.7 percent. General fund balances are expected to fall to $218.2 million, or 3.6 percent of Fiscal Year 2009 recurring appropriations absent legislative action to reduce expenditures or increase revenue. The Governor has implemented a partial hiring freeze and has required all executive agencies to prepare plans to save a minimum of 5 percent of their general fund budgets. The Governor has also requested elected public officials and the legislative and judicial branches to contribute to the overall effort to reduce expenditures. Other measures will be proposed in the 2009 legislative session to rebuild reserves to the customary target of 10 percent. These measures may include deauthorizing stalled capital outlay appropriations and cancelling some special appropriations or transferring balances in dormant funds to the General Fund. On January 12, 2009, the

Governor announced a plan to reduce State agency expenditures, improve tax collections and deauthorize capital outlay projects in order to prevent a budget shortfall in Fiscal Year 2009. Any changes to the Fiscal Year 2009 budget are expected to be addressed by the 2009 Legislature which commenced on January 20, 2009.

Fiscal Year 2010. Based upon revenue projections for Fiscal Year 2010 made in early December 2008, recurring General Fund revenues are projected to increase from Fiscal Year 2009 by 0.5 percent to $5.7 billion. The price of oil is expected to average $59.00 per barrel and natural gas is expected to average $6.35 per mcf for the fiscal year. Results and data published since December 1, 2008 suggest that the next revenue update scheduled for February 2009 will show additional weakness in both the mineral taxes and royalties and the broad-based taxes, attributable to the national recession. Per the December forecast, general and selective sales taxes are projected to grow by 1.4 percent (after adjusting for the Fiscal Year 2008/Fiscal Year 2009 accounting anomaly) while income taxes are projected to increase by 0.8 percent. The Governor has required all executive agencies to provide savings plans that reduce general fund expenditures by a minimum of 5 percent of each budget for Fiscal Year 2009; the expectation is that these savings will be carried over to the Fiscal Year 2010 budget. The announced intention is not only to balance the budget for Fiscal Year 2010, but to maintain balances at the customary 10 percent level. On January 12, 2009, the Governor announced a plan to reduce State agency expenditures, increase tax collections, increase savings from the General Services Department and the Department of Information Technology and spend General Fund reserves for Fiscal Year 2010. Also on January 12, 2009, the Legislative Finance Committee announced a $5.9 billion budget recommendation for Fiscal Year 2010, which includes lowering spending, using funds from the State's reserves and collecting new revenues. A budget for Fiscal Year 2010 is expected to be addressed by the 2009 Legislature, which commenced on January 20, 2009.

General Fund Taxes and Revenues

Programs and operations of the State are predominantly funded through a system of 28 major taxes, and a substantial number of minor taxes, administered by the Taxation and Revenue Department. The Public Regulation Commission collects taxes on insurance premiums. In addition, interest income and earnings from the Land Grant Permanent Fund and the Severance Tax Permanent Fund provide important sources of revenue for State purposes. The most important tax and revenue sources, as measured by magnitude of revenue generation, and the application of the monies to certain funds and purposes, are described below.

Gross Receipts and Compensating Taxes

The gross receipts tax is levied on the total amount of money or the value of other consideration received from selling property, tangible and certain intangible personal property in the State, from leasing property employed in the State, from performing services in the State and from research and development services performed outside the State on a product which is initially used in the State. The tax is remitted by the seller but generally passed on to the purchaser. The compensating tax is imposed generally on property used in the State but purchased elsewhere. Gross receipts and compensating taxes are due on the 25th day of the month following the month in which the transaction occurs.

The general presumption is that all receipts of a person engaging in business are subject to the gross receipts tax, even though there are over 100 specified exemptions and deductions from gross receipts taxation. Exemptions from the gross receipts tax include, but are not limited to, certain receipts of governmental agencies and certain non-profit organizations; receipts from the sale of certain vehicles; occasional sales of property or services; wages; certain agricultural products; and dividends, interest and receipts from natural gas, oil or mineral interests sales or leases. Deductions from the gross receipts tax include, but are not limited to, receipts from various types of sales or leases of tangible personal property or service; receipts from certain sales of property to governmental agencies or to certain non-profit organizations; receipts from certain processing of some agricultural products; receipts from certain publication sales; certain receipts from interstate commerce transactions; and as set forth below, certain food and medical services as of January 1, 2005.

The gross receipts and compensating taxes are together the single largest source of State General Fund revenue. The gross receipts tax is also a significant source of revenue for cities and counties. The gross receipts tax includes the 5 percent statewide gross receipts tax levy, plus several city and county local-option gross receipts taxes. Until January 1, 2005, a credit of 0.5 percent against the statewide rate of 5 percent was allowed for transactions taking place in municipalities. Receipts from the statewide gross receipts tax levy, less certain disbursements, are deposited in the State General Fund. The disbursements include 1.225 percent of the taxable gross receipts reported in each incorporated municipality to that municipality. The State Aviation Fund receives a monthly distribution equal to 4.79 percent of the reported value of jet fuel sales, and a statutory monthly distribution of $167,000. In July 2009, the monthly distribution will increase to $250,000 as specified in Section 7-1-6.7 (D) NMSA 1978. An additional $530,000 is distributed monthly to the New Mexico Finance Authority's State Building Fund Bonding Fund, pursuant to Section 7-1-6.42 NMSA 1978. After all other distributions, the General Fund share of gross receipts tax collections is about 57 percent. Receipts from the compensating tax, less distributions, are transferred to the state General Fund. Compensating tax distributions include 10 percent to the small cities assistance fund and 10 percent to the small counties assistance fund, and a distribution to municipalities based on the level of their taxable gross receipts.

In 2005, the Legislature made a number of changes to the state gross receipts tax laws in Sections 7-1-6.16, 7-1-6.46, 7-1-6.47, 7-9-92 and 7-9-93 NMSA 1978. The credit of 0.5 percent granted to municipalities against the statewide rate was eliminated. The tax on food and certain medical services also was eliminated. The legislation created a deduction for gross receipts tax from retail sales of food as defined for federal food stamp program purposes. Retailers are required to report receipts from sales of groceries and then claim a deduction for the receipts. The deduction does not apply to receipts of restaurants and sellers of prepared foods. The legislation also created a gross receipts tax deduction for some receipts of licensed health care providers (broadly defined) from Medicare Part C and managed health care plans, and health care insurers. This medical deduction was modestly expanded in the 2007 legislative session. The legislation also provides for payments from the State to reimburse local governments for lost gross receipts tax revenues. The legislation initially enacted significant penalties for improper filings, but all penalties were repealed and a credit created for past payment of penalties in the 2007 session.

In June 2008, the New Mexico Court of Appeals decided a tax dispute case, *Dell Catalog Sales L.P. v. Taxation and Revenue Dep't*, No. 26,843, which could impact the collection of New Mexico gross receipts and compensating taxes from businesses conducting commerce across jurisdictional lines by creating uncertainty regarding which jurisdiction's taxes are imposed and collected. The New Mexico Supreme Court declined to hear the case and a petition for certiorari is pending before the United States Supreme Court.

Based upon preliminary revenue results for Fiscal Year 2008, total distributions to the General Fund from gross receipts and compensating taxes grew by 0.4 percent over the previous fiscal year to $1.9 billion, comprising almost 32 percent of recurring General Fund revenue.

Personal Income Tax

The personal income tax is imposed on the net income of every individual resident and upon the net income from business, property, or employment of individual nonresidents. Collections, net of refunds, are deposited in the General Fund. State taxable income is generally equal to federal adjusted gross income less deductions and amounts not taxable by State or federal laws. The State allows deductions for income earned by Indians on reservations, graduated deductions for income earned by taxpayers 65 years or older, and deductions for low- and middle-income taxpayers.

New Mexico's personal income tax structure has changed significantly in recent years, starting in 2003. Income tax incentives were enacted to encourage economic development and investment in New Mexico, as well as to assist low and middle-income taxpayers. The Legislature enacted significant personal income tax reductions that reduced the top marginal personal income tax rate from 8.2 percent in 2002 to 4.9 percent by 2008, codified in Section 7-2-7 NMSA 1978. This law combined the Head of Household filers' tax rate with the Married, Joint and Surviving Spouse filers' tax rate, beginning in 2006. Single parents are now taxed at the same rate as married couples. Statutory changes enacted in 2005 also provided low and middle-income tax exemptions, a personal income tax exemption for medical expenses, incentives to encourage business formation in rural areas, and incentives to encourage renewable energy production in the State.

Based upon preliminary revenue results for the 2008 Fiscal Year, total distributions to the General Fund from personal income tax grew by 1.5 percent over the previous fiscal year to $1.2 billion, and generated 20 percent of total recurring General Fund revenue.

State tax rates by filing status effective Calendar Years 2008 and 2009 are set forth below:

If the taxable income is:	**Married Filing Separate:**	**If the taxable income is:**	**Surviving Spouse, Married Filing Joint and Head of Household**
Not over $4,000	1.7% of taxable income	Not over $8,000	1.7% of taxable income
$4,001 to $8,000	$68.00 plus 3.2% of excess over $4,000	$8,001 to $16,000	$136.00 plus 3.2% of excess over $8,000
$8,001 to $12,000	$196.00 plus 4.7% of excess over $8,000	$16,001 to $24,000	$392.00 plus 4.7% of excess over $16,000
Over $12,000	$384.00 plus 4.9% of excess over $12,000	Over $24,000	$768.00 plus 4.9% of excess over $24,000

If the taxable income is:	**Single Including Trust and Estates:**
Not over $5,500	1.7% of taxable income
$5,501 to $11,000	$93.50 plus 3.2% of excess over $5,500
$11,001 to $16,000	$269.50 plus 4.7% of excess over $11,000
Over $16,000	$504.50 plus 4.9% of excess over $16,000

Corporate Income Tax

The corporate income tax is imposed on the net income of a corporation doing business in the State or deriving any income from property or employment in the State by Section 7-2A-3 NMSA 1978. Collections, net of refunds, are transferred to the General Fund. Corporations are required to file a return on or before the fifteenth day of the third month following the end of each taxable year at which time corporate income taxes are also due. A corporation is required to make estimated tax payments if the tax, net of credits, is $5,000 or more. Insurance companies do not pay corporate income tax; rather, they pay a tax on insurance premiums. Nonprofit organizations and retirement trust funds also do not pay corporate income tax.

Tax rates are established under a graduated table and range from 4.8 percent on the first $500,000 or less of taxable income to 7.6 percent on income in excess of $1,000,000. Based upon preliminary revenue results for the 2008 Fiscal Year, total distributions to the General Fund of net receipts from corporate income taxes totaled $403.5 million. This is a decrease of 12.3 percent from the prior fiscal year and generated 6.7 percent of recurring General Fund revenue.

In recent years, a number of credits administered through the corporate income tax system have been enacted. These include: the film production credit, enacted pursuant to Section 7-2F-1 NMSA 1978; the real property tax credit, enacted pursuant to Section 7-2-18.10 NMSA 1978; the rural jobs tax credit, enacted pursuant to Section 7-2E-1 NMSA 1978; the biodiesel production and sale credit, enacted pursuant Section 7-2-18.21 NMSA 1978; the agricultural water conservation tax credit, enacted pursuant to 7-2-18.20 NMSA 1978; the sustainable building tax credit, enacted pursuant to Section 7-2-18.19 NMSA 1978; and the renewable energy production tax credit, enacted pursuant to Section 7-2A-19 NMSA 1978.

Mineral Production Taxes

Mineral production taxes (Resource Excise Tax, Natural Gas Processors Tax, Oil and Gas Conservation Tax, and Oil and Gas Emergency School Tax) are levied on producers and others on the value of severed minerals and material resources from within the State and these taxes are disbursed to the General Fund. The Oil and Gas Emergency School Tax is imposed for the privilege of engaging in the business of severing oil, natural gas, liquid hydrocarbons and carbon dioxide from the soil of the State. The Oil and Gas Emergency School Tax is imposed at a rate of 3.15 percent of taxable value of oil and 4 percent of taxable value for natural gas. Taxable value reflects gross sales value less deductions for royalties paid to government entities and for certain processing and transportation expenses. The same definition of taxable value is used for calculation of oil and gas severance tax liability.

Based upon preliminary revenue results for the 2008 Fiscal Year, distributions to the General Fund from Oil and Gas Emergency School Tax receipts totaled $557 million. This represents a 32.6 percent increase from the prior fiscal year. Other General Fund taxes on natural resource production totaled $69.4 million. For Fiscal Year 2008, mineral production taxes contributed 10.5 percent of recurring General Fund revenue. This is an increase from the 8.4 percent of recurring revenues for the 2007 Fiscal Year.

In 2002, the Legislature created the Jicarilla Apache Tribal Capital Improvement Tax Credit, codified in Section 7-31-27 NMSA 1978. This tax credit can reduce the Oil and Gas Emergency School Tax on products severed from wells drilled on the Jicarilla Apache Nation by up to 0.7 percent of the taxable value of production. This credit totaled $2.0 million for Fiscal Year 2008.

Royalties, Rents and Bonuses

Federal Lands. Under terms of the 1920 Federal Mineral Leasing Act, the State receives 50 percent of all income generated from leasing federal lands located in the State for mineral production. Principal sources of income are royalty payments on oil and natural gas production. Additional income is derived from bonus payments for oil and natural gas leases and royalty payments on production of coal, potash and other minerals. The U.S. Minerals Management Service collects federal mineral lease income and deducts the State’s share of administrative costs. The State receives payments on a monthly basis and makes deposits to the General Fund. Based upon preliminary revenue results for the 2008 Fiscal Year, total distributions to the General Fund from federal mineral leases totaled $564.2 million. This equals 9.4 percent of recurring General Fund receipts for the fiscal year.

Federal Fiscal Year 2008 appropriations bills implemented a 2 percent deduction from the federal royalty payments to states. This 2 percent deduction is expected to be permanent. Approximately $8 million was deducted from the federal mineral leasing payments to the State for Fiscal Year 2008 and $11 million is expected to be deducted in Fiscal Year 2009. However, since the oil and natural gas price forecasts have been significantly decreased, the value of this deduction will be less than one-half of this amount for Fiscal Year 2010.

State Lands. The State Land Office manages lands acquired by the State under the federal Fergusson Act enacted prior to statehood, as well as under the State Constitution. All income from State lands is dedicated to specific educational purposes and institutions. As with federal lands, the oil and natural gas industry is the principal source of revenue from State lands. Bonus income is also collected in the form of cash payments as a result of competitive bidding for State leases. Rentals and bonus income are distributed to the respective beneficiary institutions. The largest beneficiary group is the State's public school system. Mineral production from State trust lands also generates royalty income which is deposited in the State Land Grant Permanent Fund ("LGPF"). Royalties are imposed on most mineral production values at the rate of 12.5 percent, although there is a provision for rates of up to 20 percent for new leases on developed acreage. LGPF beneficiaries and "State lands" beneficiaries are the same: educational institutions and public schools.

Severance Tax Permanent Fund and the Land Grant Permanent Fund

The Severance Tax Permanent Fund was established in the State Treasury in 1973 to receive the residual revenues from the Bonding Fund and serve as an endowment for future capital projects. In 1976, the electorate approved a constitutional amendment giving the Severance Tax Permanent Fund constitutional status. In 1982, the electorate approved a second constitutional amendment that removed the discretionary power of the Legislature to appropriate funds from the corpus of the Severance Tax Permanent Fund. Distributions from investments of the Severance Tax Permanent Fund, however, may be appropriated by the Legislature in the same manner as other general revenues are appropriated. Severance tax receipts have been the primary source of funding for the Severance Tax Permanent Fund. The State Investment Officer under the direction of the State Investment Council ("SIC") invests the corpus and non-appropriated income of the Severance Tax Permanent Fund. The market value of the Severance Tax Permanent Fund as of June 30, 2008 was approximately $4.3 billion, a decrease of approximately 9 percent from the prior fiscal year. Since the end of Fiscal Year 2008, this fund has experienced a material loss in value related to the downturn in the nation's economy. For the quarter ended September 30, 2008, the SIC estimates losses of approximately 7.9 percent in the Severance Tax Permanent Fund. For the year ended September 30, 2008, the SIC estimates losses of approximately 13.3 percent in the Severance Tax Permanent Fund. For the quarter ended December 31, 2008, the SIC had losses of approximately 19.5 percent in the Severance Tax Permanent Fund. Money on deposit in the Severance Tax Permanent Fund is not pledged to and may not be used to pay any Bonds.

The LGPF is designed solely to benefit the public educational system of the State and other specified institutions. The origins of the LGPF are found in the Fergusson Act of 1898, which granted two sections of land in every township for the benefit of the public schools in the territories of New Mexico. Also under this Act, specific acreage was granted to individual education, medical and penal institutions in the territory. The initial grant totaled in excess of 5.5 million acres. In 1910, the Enabling Act granted additional lands to various beneficiaries in New Mexico, including the public schools, with the latter receiving the largest share. This brought the total lands placed in trust for the common school system and other beneficiaries to over 13 million acres. Over the years, some land has been sold (and the proceeds used to increase the corpus of the LGPF), so the current total is nine million surface acres and 12.8 million subsurface acres.

Pursuant to Section 19-1-1 NMSA 1978, the State Land Office is charged with the custody and disposition of the land granted to the State. The Commissioner of Public Lands sells or leases these properties in accordance with the provisions of the appropriate statutes. The State Investment Officer under the direction of the SIC invests the corpus and income of the LGPF. As of June 30, 2008, the market value of the LGPF was approximately $10.1 billion, a decrease of approximately 5 percent from the prior fiscal year. For the quarter ended September 30, 2008, the SIC estimates losses of approximately 7.5 percent in the LGPF. For the year ended September 30, 2008, the SIC estimates losses of approximately 12.6 percent in the LGPF. For the quarter ended December 31, 2008, the SIC had losses of approximately 18 percent in the LGPF. The corpus of the LGPF is constitutionally protected from appropriation and amounts on deposit therein are not pledged to and may not be used to pay debt. The LGPF is also protected by the Federal Enabling Act of 1910.

In November 1996, the State electorate approved a constitutional amendment regarding distributions from both of the State's permanent funds. Distributions are now based on a total return basis rather than an income distribution method. In addition, distributions to beneficiaries are now based on a formula under which 4.7 percent of the previous average five-year market value of the fund is distributed.

In September 2003, the State electorate approved a constitutional amendment increasing the rate of distribution from the LGPF from 4.7 percent to 5 percent of the five-year average market value of the LGPF beginning in Fiscal Year 2005. Certain additional distributions shall be made to implement and maintain educational reforms as provided by law. An additional 0.8 percent has been and will be distributed in Fiscal Years 2005 through 2012 and an additional 0.5 percent will be distributed in Fiscal Years 2013 through 2016. A three-fifths majority of each house of the Legislature may suspend this additional distribution.

Investment Income

Investment earnings are generated from three primary sources: the LGPF, the Severance Tax Permanent Fund, and cash balances held by the State Treasurer. Income from the LGPF is distributed among the beneficiary institutions and public schools. The dedication received by the public schools, which is approximately 83 percent, is deposited in the General Fund. Based on preliminary revenue results for the 2008 Fiscal Year, $390.5 million of LGPF distributions were transferred to the General Fund for public school purposes. The State distributed $177.2 million of income from the Severance Tax Permanent Fund, all of which was deposited in the General Fund. In the 2008 Fiscal Year, the Treasurer's cash balances produced $55.9 million for the General Fund, net of the issuance and interest cost of the Tax and Revenue Anticipation Notes (TRAN). Total investment income credited to the General Fund was $623.6 million. This is 10.4 percent of recurring General Fund receipts.

PROPERTY VALUATION AND TAXATION

The valuation of oil and gas production and the assessment of the *ad valorem* production tax are based on the actual value of production on a monthly basis from September 1 to August 31. Oil and natural gas are valued for the calendar year preceding the property tax year, as explained in Section 7-32-15 NMSA 1978. For rate setting, the Local Government Division of the DFA may adjust the State levy for changes in oil and natural gas values.

In November 1998, the New Mexico electorate approved an amendment to Section 1 of Article VIII of the State Constitution to authorize the Legislature to limit increases in residential property valuation for property taxes. The limitation may be applied to classes of residential property taxpayers based on owner-occupancy, age or income. The limitations may be authorized statewide or at the option of a local jurisdiction and may include conditions. Any valuation limitations authorized as a local jurisdiction option shall provide for applying statewide or multi-jurisdictional property tax rates to the value of the property as if the valuations increase limitation did not apply. This amendment and related legislation may have an impact on future property taxation increases.

The 2000 Legislature passed and the Governor signed legislation limiting the increase in the value of residential property for property valuation purposes. Section 7-36-21.3 NMSA 1978 provides for a freezing of values for single-family dwellings occupied by certain low-income owners 65 years of age or older. Another law provides that the value of a residential property in any tax year, starting with the year 2001, shall not exceed certain percentage increases based on whether the county where the property is situated has a sales assessment ratio of at least 85 percent, as codified in Section 7-36-21.2 NMSA 1978. Sales assessment ratios are computed annually by the Taxation and Revenue Department and measure a county's assessment valuations against current sales information. Counties that have at least an 85 percent sales assessment ratio are considered "current and correct" while counties that fall below that threshold are considered not "current and correct." If a property is situated in a current and correct county, the law limits the annual increase to no more than 3 percent (and 6.1 percent over the value two years ago). If a property is situated in a county that is not current and correct, the law limits the annual increase to 5 percent. In addition, in such a non-current and correct county, the law limits the aggregate annual increases for all properties (excluding net new properties added to the tax rolls) in that county to 3 percent. The annual limitations do not apply to new improvements or to any property that has had a change in ownership, use or zoning during the year.

The 2005 Legislature passed and the Governor signed a bill, codified as Section 7-38-12.1 NMSA 1978 of the Property Tax Code, requiring the disclosure only to the County Assessor of sale prices and other items of value upon the sale of residential real property. This amendment has led to an increase in the assessed value of some residential properties. Table 17 sets forth the aggregate statewide net taxable valuations for the last 10 years.

TABLE 17
Final Net Taxable Valuations
(Dollars in thousands)

Property Tax Year	Residential	Non-Residential	Oil and Gas	Copper	Net Taxable Value
1999	$14,660,993	$9,311,907	$1,852,447	$192,897	$26,018,245
2000	15,311,042	9,946,121	2,166,427	160,906	27,584,497
2001	16,336,147	10,209,818	4,238,592	117,376	30,901,933
2002	17,133,856	10,336,906	3,024,570	–	30,495,332
2003	18,279,692	10,778,559	3,024,570	66,614	32,149,435
2004	19,421,800	10,839,281	5,563,785	65,157	35,890,023
2005	21,120,378	12,161,447	4,643,270	65,157	38,910,768
2006	23,016,630	12,605,105	7,259,891	103,402	42,985,028
2007	25,805,629	14,458,192	5,758,696	133,262	47,288,631
2008	27,798,246	15,259,324	7,245,955	160,279	50,463,804

Source: New Mexico Department of Finance and Administration, Local Government Division.

Production and Property Taxes on Oil and Natural Gas

The Oil and Gas Emergency School Tax Act, Section 7-31-1 et seq. NMSA 1978 taxes oil and certain gases at 3.15 percent and natural gas 4.0 percent. The Oil and Gas Severance Tax Act, Section 7-29-4(A) NMSA 1978, imposes a 3.75 percent tax on both oil and natural gas. The Oil and Gas Conservation Tax Act, Section 7-30-4(A) NMSA 1978, taxes both oil and natural gas at 0.19 percent. Statutory tax rates are effectively reduced by deductions for royalties paid to governments and for certain transportation expenses. The *ad valorem* taxes are imposed in lieu of property taxes on reserves and lease equipment, and local rates vary in accordance with jurisdiction.

The 2005 Legislature amended severance tax laws to include helium and hydrocarbon gases in the definition of products subject to the oil and gas severance tax, the oil and gas conservation tax, the oil and gas school emergency tax and the oil and gas production *ad valorem* tax.

Current effective production and property tax rates expressed on *ad valorem* and unit bases are shown below. The rates were based on data from Fiscal Year 2008 and reflect an average sales price of $92.61 per barrel for oil and $8.23 per thousand cubic feet ("mcf") for natural gas. The effective rates presented in Table 18 show taxes paid as a percentage of gross sales value before subtracting allowable deductions.

TABLE 18
Effective Tax Rates applicable for Fiscal Year 2008

	Crude Oil		**Natural Gas**	
Type of Tax	**Ad Valorem**	**Per Barrel**	**Ad Valorem**	**Per mcf**
Price		**$92.61**		**$8.23**
Oil and Gas School Tax	2.83%	$2.57	3.27%	$0.27
Oil and Gas Severance Tax	3.38%	$3.07	3.10%	$0.26
Oil and Gas Conservation Tax (General Fund only)	0.153%	$0.14	0.14%	$0.01
Oil and Gas Conservation Tax (Reclamation)	0.018%	$0.016	0.017%	$0.00
Natural Gas Processors Tax	N/A	N/A	0.35%	$0.04
Oil and Gas Production *ad valorem* Tax	1.04%	$0.95	0.90%	$0.07
Oil and Gas Production Equipment *ad valorem* Tax	0.15%	$0.14	0.14%	$0.01
Total	**7.58%**	**$6.88**	**7.92%**	**$0.62**
Subtotal: State Tax Only (excludes *ad valorem* taxes)	6.38%	$5.79	6.88%	$0.58

Source: New Mexico Department of Finance and Administration.

Production, Sales, and Property Taxes on Coal

The average burden of production and property taxes on a ton of coal produced and sold during Fiscal Year 2008 is shown in Table 19:

TABLE 19
Tax Burden

Type of Tax	**Tax Burden Effective Rate**	**Amount[(1)]**
Severance Tax and Surtax		
Net of ITC	$0.75 per ton	$ 17,194,895
Resources Excise Tax	0.19 per ton	4,432,200
Conservation Tax	0.05 per ton	1,133,085
Property Tax[(2)]	0.27 per ton	6,071,098
Gross Receipts Tax	1.55 per ton	35,369,395
Total	**$2.82 per ton**	**$64,200,673**
Price Per Ton		**$ 28.72**
Total Production		**22,801,290**
Total Value		**$ 654,942,711**

(1) The figures reported in this table come from the New Mexico Taxation and Revenue Department's GenTax System. They reflect only the information contained in all tax returns and amendments filed during Fiscal Year 2008. These figures differ from actual distributions made by the Taxation and Revenue Department's Financial Services Bureau, as the distributions include penalties, interest, and other modifications such as previously unallocated or unidentified receipts.

(2) Property taxes were billed in calendar year 2007 and collected in Fiscal Year 2008.

Source: New Mexico Taxation and Revenue Department, Tax Analysis, Research and Statistics Office (the GenTax System, Financial Services Bureau and Property Tax Division's Central Assessment Unit).

Statutory rates for the resources excise tax and the conservation tax are effectively reduced by a deduction for Federal, State and Indian royalties. The effective severance tax rate on coal reflects the mix of old and new contract sales and of underground and surface mines. Property tax pertains to both equipment and production values. Fundamental differences in tax bases preclude a true comparison between property taxes and other taxes shown above. However, property taxes are included in this analysis to prevent understating the tax burden.

In addition to production taxes, gross receipts tax is imposed on coal produced and sold within the State. From January to September of 2008, 69 percent of all coal produced in the State and supplied to electricity generating stations was supplied to power plants in New Mexico. The remaining 31 percent was transported by rail to electricity generators in Arizona. 94 percent of all coal produced in New Mexico is subject to the gross receipts tax. The combined state and local tax rate is 6.2495 percent of value. To convert taxes per unit of output to tax rates per dollar of sales, the taxes shown above may be divided by the average price per ton of coal in Fiscal Year 2008, which was $28.72.

Excluding Gross Receipts Tax	3.45%
Including Gross Receipts Tax	9.82%