

New Issue

This Official Statement has been prepared by the State Board of Finance to provide information on the \$37,040,000 State of New Mexico Severance Tax Bonds, Refunding Series 2005B-1 (the "Series 2005B-1 Bonds") and the \$21,095,000 Supplemental Severance Tax Bonds, Refunding Series 2005B-2 (the "Series 2005B-2 Bonds" and collectively with the Series 2005B-1 Bonds, the "Bonds"). Selected information is presented on this cover page for the convenience of the user. To make an informed decision, a prospective investor should read the entire Official Statement. Certain capitalized terms used in the cover page and elsewhere in this Official Statement have the meanings given in the Official Statement.

\$58,135,000

THE STATE OF NEW MEXICO

\$37,040,000 SEVERANCE TAX BONDS, REFUNDING SERIES 2005B-1

\$21,095,000 SUPPLEMENTAL SEVERANCE TAX BONDS, REFUNDING SERIES 2005B-2

Dated: Delivery Date

Due: July 1, as shown below

*Ratings on Series 2005B-1
Bonds*

"AA2" Moody's Investors Services, Inc.

"AA" Standard & Poor's Ratings Service, a division of The McGraw-Hill Companies, Inc.

*Ratings on Series 2005B-2
Bonds-Ambac Insured*

"Aaa" Moody's Investors Services, Inc.

"AAA" Standard & Poor's Ratings Service, a division of The McGraw-Hill Companies, Inc.

*Underlying Ratings on
Series 2005B-2 Bonds*

"AA3" Moody's Investors Services, Inc.

"A+" Standard & Poor's Ratings Service, a division of The McGraw-Hill Companies, Inc.

Tax Exemption

In the opinion of Sutin, Thayer & Browne A Professional Corporation, Bond Counsel, based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Bonds is excludable from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, such interest is taken into account in determining adjusted current earnings for the purpose of computing the alternative minimum tax on certain corporations. Bond Counsel is further of the opinion that interest on the Bonds is exempt from State of New Mexico personal income taxes. Bond Counsel expresses no opinion regarding any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Bonds. See "TAX MATTERS."

*No Optional Redemption
Bond Insurance*

The Bonds are not subject to optional redemption prior to maturity.

The scheduled payment of principal and interest on the Series 2005B-2 Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Series 2005B-2 Bonds by Ambac Assurance Corporation.

Sources of Payment

The Bonds are payable primarily from, and secured by, taxes levied upon certain natural resource products severed and saved from the soil of the State deposited into the Severance Tax Bonding Fund.

Priority

The Bonds are being issued under the authority of the State of New Mexico Severance Tax Bonding Act. The Series 2005B-1 Bonds will be on a parity with Severance Tax Bonds now or hereafter outstanding and senior to Supplemental Severance Tax Bonds now or hereafter outstanding. The Series 2005B-2 Bonds will be on a parity with Supplemental Severance Tax Bonds now or hereafter outstanding and subordinate to Severance Tax Bonds now or hereafter outstanding.

Purposes

Net proceeds of the Series 2005B-1 Bonds are being used to advance refund certain outstanding maturities of the State of New Mexico Severance Tax Bonds, Refunding Series 2001A and Series 2002A (collectively, the "Senior Refunded Bonds"). Net proceeds of the Series 2005B-2 Bonds are being used to advance refund certain outstanding maturities of the State of New Mexico Supplemental Severance Tax Bonds, Series 2002A (collectively the "Supplemental Refunded Bonds" and together with the Senior Refunded Bonds, the "Refunded Bonds").

Interest Payment Dates

January 1 and July 1, commencing January 1, 2006

Closing/Settlement

On or about June 28, 2005

Denominations

\$5,000

Book-Entry System

The Depository Trust Company

Registrar/Paying Agent

State Treasurer of New Mexico

Bond Counsel

Sutin, Thayer & Browne A Professional Corporation

Disclosure Counsel

Brownstein Hyatt & Farber, P.C.

Underwriters' Counsel

McCall Parkhurst & Horton L.L.P. and Scheuer, Yost & Patterson, PC

Issuer Contact

State Board of Finance; 505-827-4980; [sstovall@state.nm.us](mailto:ssstovall@state.nm.us)

RBC Dain Rauscher
Goldman, Sachs & Co.
Popular Securities

Banc of America Securities LLC
Piper Jaffray & Co.
Siebert Brandford Shank & Co.

Dated: May 24, 2005

Series 2005B-1 Bonds

<u>CUSIP</u>	<u>Year (July 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield at Issuance</u>	<u>Price at Issuance</u>	<u>Initial Call Date</u>	<u>Price</u>
647310A27	2008	\$5,405,000	5.000%	2.980%	105.771%	Not callable	-
647310B42	2008	505,000	3.000%	2.980%	100.056%	Not callable	-
647310A35	2009	7,215,000	5.000%	3.070%	107.226%	Not callable	-
647310B59	2009	1,250,000	3.250%	3.070%	100.673%	Not callable	-
647310A43	2010	5,805,000	5.000%	3.190%	108.316%	Not callable	-
647310B67	2010	1,405,000	3.250%	3.190%	100.275%	Not callable	-
647310A50	2011	6,545,000	5.000%	3.300%	109.196%	Not callable	-
647310B75	2011	1,000,000	3.500%	3.300%	101.081%	Not callable	-
647310A68	2012	6,800,000	5.000%	3.410%	109.837%	Not callable	-
647310B83	2012	1,110,000	3.500%	3.410%	100.556%	Not callable	-

Series 2005B-2 Bonds

<u>CUSIP</u>	<u>Year (July 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield at Issuance</u>	<u>Price at Issuance</u>	<u>Initial Call Date</u>	<u>Price</u>
647310A76	2009	\$6,510,000	5.000%	3.040%	107.343%	Not callable	-
647310C33	2009	250,000	3.250%	3.040%	100.786%	Not callable	-
647310A84	2010	6,675,000	5.000%	3.160%	108.461%	Not callable	-
647310C41	2010	350,000	3.250%	3.160%	100.413%	Not callable	-
647310A92	2011	7,085,000	5.000%	3.280%	109.310%	Not callable	-
647310C58	2011	225,000	3.500%	3.280%	101.190%	Not callable	-

No dealer, salesman or other person has been authorized by the State of New Mexico (the "State") or the Underwriters to give any information or to make any statements or representations, other than those contained in this Official Statement, and, if given or made, such other information, statements or representations must not be relied upon as having been authorized. This Official Statement does not constitute an offer to sell or solicitation of an offer to buy any of the Bonds in any jurisdiction in which such offer or solicitation is not authorized, or in which any person making such offer or solicitation is not qualified to do so, or to any person to whom it is unlawful to make such offer or solicitation in such jurisdiction. The information set forth or included in this Official Statement has been provided by the State and from other sources believed by the State to be reliable. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale hereunder shall create any implication that there has been no change in the financial condition or operations of the State described herein since the date hereof. This Official Statement contains, in part, estimates and matters of opinion that are not intended as statements of fact, and no representation or warranty is made as to the correctness of such estimates and opinions or that they will be realized.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

The Bonds have not been registered under the Securities Act of 1933 in reliance upon exemptions contained in such Act. The registration and qualification of the Bonds in accordance with applicable provisions of the securities law of the states in which the Bonds have registered or qualified and the exemption from registration or qualification in other states cannot be regarded as a recommendation thereof. Neither the Securities and Exchange Commission nor any other federal, state, municipal or other governmental entity, nor any agency or department thereof, has passed upon the merits of the Bonds or the accuracy or completeness of this Official Statement. Any representation to the contrary may be a criminal offense.

This Official Statement is "deemed final" by the State for purposes of Rule 15c2-12 of the Municipal Securities Rulemaking Board. The State has covenanted to provide such annual financial statements and other information in the manner as may be required by regulations of the Securities and Exchange Commission or other regulatory body.

This Official Statement contains statements that are "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. When used in this Official Statement, the words "estimate," "project," "intend," "expect" and similar expressions are intended to identify forward-looking statements. Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof.

THE PRICES AT WHICH THE BONDS ARE OFFERED TO THE PUBLIC BY THE UNDERWRITERS (AND THE YIELDS RESULTING THEREFROM) MAY VARY FROM THE INITIAL PUBLIC OFFERING PRICES OR YIELDS APPEARING ON THE INSIDE COVER PAGE HEREOF. IN ADDITION, THE UNDERWRITERS MAY ALLOW CONCESSIONS OR DISCOUNTS FROM SUCH INITIAL PUBLIC OFFERING PRICES TO DEALERS AND OTHERS. IN CONNECTION WITH THE OFFERING OF THE BONDS, THE UNDERWRITERS MAY EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICE OF THE BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

IN MAKING AN INVESTMENT DECISION INVESTORS MUST RELY ON THEIR OWN EXAMINATION OF THE STATE AND THE TERMS OF THE OFFERING, INCLUDING THE MERITS AND RISKS INVOLVED. THESE SECURITIES HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS DOCUMENT. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

ELECTED STATE OFFICIALS

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REBECCA D. VIGIL-GIRON
Secretary of State

DIANE D. DENISH
Lieutenant Governor

ROBERT E. VIGIL
State Treasurer

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State Auditor

PATRICIA A. MADRID
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Commissioner of Public Lands

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JASON A. MARKS
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District III

LYNDA LOVEJOY
District IV

E. SHIRLEY BACA
District V

STATE BOARD OF FINANCE

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President

LT. GOVERNOR
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ROBERT E. VIGIL
Member

Appointed Members

PAUL BLANCHARD
Secretary

KIM SANCHEZ RAEI
Member

MARIA GRIEGO-RABY
Member

ROBERTA COOPER RAMO
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Swarthmore, Pennsylvania
Public Resources Advisory Group
Los Angeles, California

SUMMARY OF INFORMATION
SEVERANCE TAX BONDS, REFUNDING SERIES 2005B-1
SUPPLEMENTAL SEVERANCE TAX BONDS, REFUNDING SERIES 2005B-2

The following material represents a summary of information concerning the Bonds and the security therefor set forth in this Official Statement and is qualified in its entirety by the detailed information herein. Purchasers of the Bonds should review the entire Official Statement making an investment decision.

Dated:	Delivery Date.
Interest Payment:	Interest is payable semi-annually on January 1 and July 1, commencing on January 1, 2006.
Principal Payment:	The Bonds mature in serial installments as set forth on the inside cover page of this Official Statement.
No Optional Redemption:	The Bonds are <u>not</u> subject to optional redemption prior to maturity.
Bond Insurance:	The scheduled payment of principal and interest on the Series 2005B-2 Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Series 2005B-2 Bonds by Ambac Assurance Corporation.
Registration:	The Bonds are being issued solely in book-entry form in the denomination of \$5,000 or any integral multiple thereof. The Bonds are being registered to Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York, which will act as depository.
Legal Opinion:	The Bonds are offered when, as and if issued, subject to the approval of legality by Sutin, Thayer & Browne A Professional Corporation, Bond Counsel.
Security:	The Bonds constitute special obligations of the State of New Mexico and will be payable solely from deposits to and revenues of the Severance Tax Bonding Fund, consisting primarily of receipts from certain taxes levied on certain natural resource products severed and saved from the soil of the State of New Mexico as more fully described herein.
Additional Parity Bonds:	The State Board of Finance is prohibited by statute from issuing Senior Severance Tax Bonds unless the aggregate amount of Senior Severance Tax Bonds outstanding, including the bonds to be issued, can be serviced with not more than 50 percent of the annual deposits into the Severance Tax Bonding Fund, as determined by the deposits during the preceding Fiscal Year. The State Board of Finance is prohibited by statute from issuing Supplemental Severance Tax Bonds unless the aggregate amount of Senior and Supplemental Severance Tax Bonds outstanding, including the bonds to be issued, can be serviced with not more than 62.5 percent of the annual deposits into the Severance Tax Bonding Fund, as determined by the deposits during the preceding Fiscal Year.

Summary of Projected and Historical Coverage in Severance Tax Bonding Fund
Fiscal Year Ended June 30
(Dollars in thousands)

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Projected Bonding Fund Receipts	\$362,791	\$332,158	\$318,062	\$301,466	\$292,341
Senior Bond Debt Service ⁽¹⁾⁽²⁾	\$68,204	\$70,863	\$69,700	\$61,891	\$59,767
Senior Bond Debt Service Coverage Ratio	5.32x	4.69x	4.56x	4.87x	4.89x
Supplemental Bond Debt Service ⁽¹⁾⁽²⁾	\$19,008	\$20,243	\$20,119	\$18,020	\$15,899
Supplemental Bond Debt Service Coverage Ratio	4.16x	3.65x	3.54x	3.77x	3.86x
	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Bonding Fund Receipts	\$196,763	\$356,261	\$246,046	\$257,157	\$319,337
Senior Bond Debt Service ⁽²⁾	\$69,924	\$68,227	\$72,893	\$67,994	\$68,270
Senior Bond Debt Service Coverage Ratio	2.81x	5.22x	3.38x	3.78x	4.68x
Supplemental Bond Debt Service	\$0	\$2,101	\$4,026	\$12,757	\$18,230
Supplemental Bond Debt Service Coverage Ratio	-	5.07x	3.20x	3.18x	3.69x

⁽¹⁾ Includes debt service on the Bonds and gives effect to the issuance of the Series 2005A Bonds.

⁽²⁾ Excludes debt service on advance refunded bonds which will be paid from escrowed securities and severance tax debt obligations sold to the State Treasurer which are retired within the same Fiscal Year.

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\$58,135,000
THE STATE OF NEW MEXICO
\$37,040,000 SEVERANCE TAX BONDS, REFUNDING SERIES 2005B-1
\$21,095,000 SUPPLEMENTAL SEVERANCE TAX BONDS, REFUNDING SERIES 2005B-2

INTRODUCTION

The purpose of this portion of this Official Statement, including the cover page, the Summary of Information, and the Appendices hereto, is to furnish information regarding the issuance of the Severance Tax Bonds, Refunding Series 2005B-1 in the principal amount of \$37,040,000 (the "Series 2005B-1 Bonds"), the issuance of the Supplemental Severance Tax Bonds, Refunding Series 2005B-2 in the principal amount of \$21,095,000 ("Series 2005B-2 Bonds" and collectively with the Series 2005B-1 Bonds, the "Bonds"), the State of New Mexico (the "State"), and the State Board of Finance (the "Board").

The Bonds are being issued under authority of the State Severance Tax Bonding Act, Sections 7-27-1 through 7-27-27 NMSA 1978 as amended (the "Severance Tax Bonding Act") and pursuant to a resolution of the Board adopted on May 24, 2005 (the "Bond Resolution").

This Official Statement contains summaries of the terms of the Bonds, certain fiscal matters of the State and the Severance Taxes (defined below) imposed by the State. The descriptions included in this Official Statement do not purport to be comprehensive or definitive, and such summaries and descriptions are qualified in their entirety by reference to such laws, and the definitive forms of documents, exhibits or appendices where applicable.

Requests for additional information about the State, the Severance Taxes, or requests for copies of any document or statute referred to in this Official Statement, may be directed to:

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THE SEVERANCE TAX BONDS

General Terms

The Bonds are dated their date of delivery, bear interest until the principal amount thereof is paid, and mature as set forth on the inside cover page hereof. Interest on the Bonds is payable on January 1 and July 1, commencing on January 1, 2006. The Bonds are being issued solely in book-entry form in denominations of \$5,000 or an integral multiple thereof. The Bonds are being registered in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York, which will act as depository for the Bonds. The Bonds are subject to transfer and exchange as set forth in the Bond Resolution.

No Optional Redemption

The Bonds will not be subject to redemption prior to their maturity dates.

Security for the Bonds

There are two categories of bonds issued by the State Board of Finance wherein the money in the Severance Tax Bonding Fund (the “Bonding Fund”) is pledged for their retirement. Those bonds are referred to in the Severance Tax Bonding Act as “New Mexico Severance Tax Bonds” and as “New Mexico Supplemental Severance Tax Bonds” but are referred to herein as “Senior Severance Tax Bonds” and “Supplemental Severance Tax Bonds,” respectively. Where appropriate, Senior Severance Tax Bonds and Supplemental Severance Tax Bonds are collectively referred to herein as “Severance Tax Bonds.”

Security for the Series 2005B-1 Bonds

Pursuant to the Severance Tax Bonding Act the Board is prohibited by statute from issuing Senior Severance Tax Bonds unless the aggregate amount of total Senior Severance Tax Bonds outstanding, including the bonds to be issued, can be serviced with not more than 50 percent of the annual deposits into the Bonding Fund, as determined by the deposits during the State’s preceding Fiscal Year. The total aggregate principal amount of outstanding Severance Tax Bonds issued by the State does not now, nor will such amount upon the issuance of the Bonds, exceed any applicable limit prescribed by the Constitution or laws of the State.

The Series 2005B-1 Bonds, all currently outstanding Senior Severance Tax Bonds, and any Senior Severance Tax Bonds issued on a parity with the Series 2005B-1 Bonds will have a pledge and lien senior to any Supplemental Severance Tax Bonds now outstanding or hereafter issued.

The Series 2005B-1 Bonds are special obligations of the State secured by and payable solely from, on a parity basis to Senior Severance Tax Bonds now or hereafter outstanding and on a prior lien basis to Supplemental Severance Tax Bonds now or hereafter outstanding, deposits to the Bonding Fund into which are deposited, pursuant to the Severance Tax Bonding Act, the net receipts from taxes levied in accordance with the Severance Tax Act and the Oil and Gas Severance Tax Act upon certain natural resource products severed and saved from the soil of the State (“Severance Taxes”), investment earnings on such deposits and on unused bond proceeds in certain accounts, and such other moneys as the Legislature in its sole discretion may from time to time determine. On June 30 and December 31 of each year, the excess money in the Bonding Fund over the amount necessary to meet all principal and interest payments on all outstanding Severance Tax Bonds on the next two ensuing semiannual payment dates must be transferred to the Severance Tax Permanent Fund.

Once moneys are so transferred, they no longer may be used to pay, or to secure payment of, principal of, premium, if any, or interest on any Severance Tax Bonds. Severance Tax Bonds are not general obligations of the State and the State is prohibited by law from using the proceeds of property taxes as a source of payment of revenue bonds, including Severance Tax Bonds. The State Treasurer keeps separate accounts for all money collected as Severance Taxes, and is directed by State statute to pay Severance Tax Bonds from moneys on deposit in the Bonding Fund. The Bond Resolution provides for the creation of a separate Debt Service Account within the Bonding Fund for the payment of principal and interest on the Bonds.

The Severance Tax Bonding Act requires the Legislature to provide for the continued assessment, levy, collection and deposit into the Bonding Fund of Severance Taxes which, together with such other

moneys as may be deposited into the Bonding Fund, will be sufficient to produce an amount at least equal to annual debt service on all outstanding Severance Tax Bonds.

In addition, the Board covenants in the Bond Resolution that the State will use its best efforts to collect and deposit in the Bonding Fund sufficient income from Severance Taxes so that, when combined with other moneys deposited in the Bonding Fund, the amount deposited annually in the Bonding Fund will equal at least 200 percent of the amount of the principal and interest scheduled to be due in each Fiscal Year on all Senior Severance Tax Bonds, including the Series 2005B-1 Bonds. However, the Board does not have the power to levy or impose Severance Taxes, and no assurance exists that the 200 percent requirement will be met.

Security for the Series 2005B-2 Bonds

The Board also is prohibited by statute from issuing Supplemental Severance Tax Bonds unless the aggregate amount of total Senior Severance Tax Bonds and Supplemental Severance Tax Bonds outstanding, including the Supplemental Severance Tax Bonds to be issued, can be serviced with not more than 62.5 percent of the annual deposits into the Bonding Fund, as determined by the deposits during the State's preceding Fiscal Year. The total aggregate principal amount of outstanding Severance Tax Bonds issued by the State does not now, nor will such amount upon the issuance of the Bonds, exceed any applicable limit prescribed by the Constitution or laws of the State.

The Series 2005B-2 Bonds, all currently outstanding Supplemental Severance Tax Bonds, and any Supplemental Severance Tax Bonds issued on a parity with the Series 2005B-2 Bonds, will have a pledge and lien on a parity with the Series 2005B-2 Bonds, the outstanding Supplemental Severance Tax Bonds and any other Supplemental Severance Tax Bonds hereafter issued and subordinate to any Senior Severance Tax Bonds now outstanding or hereafter issued.

The Series 2005B-2 Bonds are special obligations of the State secured by and payable solely from, on a basis subordinate to Senior Severance Tax Bonds now or hereafter outstanding and on a parity basis to Supplemental Severance Tax Bonds now or hereafter outstanding, deposits to the Bonding Fund into which are deposited, pursuant to the Severance Tax Bonding Act, the net receipts from Severance Taxes, investment earnings on such deposits and on unused bond proceeds in certain accounts, and such other moneys as the Legislature in its sole discretion may from time to time determine. On June 30 and December 31 of each year, the excess money in the Bonding Fund over the amount necessary to meet all principal and interest payments on all outstanding Severance Tax Bonds on the next two ensuing semiannual payment dates must be transferred to the Severance Tax Permanent Fund.

Once moneys are so transferred, they no longer may be used to pay, or to secure payment of, principal of, premium, if any, or interest on any Severance Tax Bonds. Severance Tax Bonds are not general obligations of the State and the State is prohibited by law from using the proceeds of property taxes as a source of payment of revenue bonds, including Severance Tax Bonds. The State Treasurer keeps separate accounts for all money collected as Severance Taxes, and is directed by State statute to pay Severance Tax Bonds from moneys on deposit in the Bonding Fund. The Bond Resolution provides for the creation of a separate Debt Service Account within the Bonding Fund for the payment of principal and interest on the Bonds.

The Severance Tax Bonding Act requires the Legislature to provide for the continued assessment, levy, collection and deposit into the Bonding Fund of Severance Taxes which, together with such other moneys as may be deposited into the Bonding Fund, will be sufficient to produce an amount at least equal to annual debt service on all outstanding Severance Tax Bonds.

In addition, the Board covenants in the Bond Resolution that the State will use its best efforts to collect and deposit in the Bonding Fund sufficient income from Severance Taxes so that, when combined with other moneys deposited in the Bonding Fund, the amount deposited annually in the Bonding Fund will equal at least 160 percent of the amount of the principal and interest scheduled to be due in each Fiscal Year on all Senior Severance Tax Bonds, the Series 2005B-2 Bonds and other Supplemental Severance Tax Bonds. However, the Board does not have the power to levy or impose Severance Taxes, and no assurance exists that the 160 percent requirement will be met.

PLAN OF FINANCING

Purpose

The purpose of the advance refunding is to achieve annual and present value savings on certain outstanding maturities of the State's Senior Severance Tax Bonds and Supplemental Severance Tax Bonds.

Bonds to be Refunded

The Series 2005B-1 Bonds are being used to provide funds for the advance refunding of the State of New Mexico, Severance Tax Bonds, Refunding Series 2001A (July 1, 2008, and 2009 maturities) and Series 2002A (July 1, 2009, 2010, 2011 and 2012 maturities) (collectively the "Senior Refunded Bonds"). Proceeds of the Series 2005B-1 Bonds will be used to fund an escrow account pursuant to an Escrow Agreement that will provide for payments of interest on the Senior Refunded Bonds from the closing of the Series 2005B-1 Bonds to their respective earliest call date of the Senior Refunded Bonds as well as for the redemption of the Senior Refunded Bonds at their earliest respective call date.

The Series 2005B-2 Bonds are being used to provide funds for the advance refunding of the State of New Mexico, Supplemental Severance Tax Bonds, Series 2002A (July 1, 2009, 2010 and 2011 maturities) (collectively the "Supplemental Refunded Bonds" and together with the Senior Refunded Bonds, the "Refunded Bonds"). Proceeds of the Series 2005B-2 Bonds will be used to fund an escrow account pursuant to an Escrow Agreement that will provide for payments of interest on the Supplemental Refunded Bonds from the closing of the Series 2005B-2 Bonds to their respective earliest call date of the Supplemental Refunded Bonds as well as for the redemption of the Supplemental Refunded Bonds at their earliest respective call date.

Refunding and Defeasance

The proceeds of the Bonds will be deposited into the Escrow Accounts for the Senior Refunded Bonds and the Supplemental Refunded Bonds, respectively, pursuant to an Escrow Agreement among the State, the State Treasurer as paying agent, registrar and authenticating agent for the Refunded Bonds and Wells Fargo Bank, N.A., as Escrow Agent, in amount sufficient, together with investment income thereon, to pay the principal of and interest on the Refunded Bonds as set forth below in the Summary of Refunded Bonds.

Moneys in the Escrow Accounts established under the Escrow Agreement for the payment of the Refunded Bonds may be invested, as provided in the Escrow Agreement, in the following classes of securities: (i) direct obligations of, or obligations as to full and timely payment of principal and interest on which is unconditionally guaranteed by, the United States of America; (ii) obligations issued or guaranteed as to full and timely payment of principal and interest by an agency or person controlled by and acting as an instrumentality of the United States of America, pursuant to authority granted by Congress of the United States of America; and (iii) obligations described in Section 103(a) of the Code

(a) provisions for the payment of the principal of, premium, if any, and interest on which (1) shall have been made by the irrevocable deposit, with a bank or trust company acting as a trustee or escrow agent for holders of such obligations, of noncallable securities described in clauses (i) and (ii) above, the maturing principal of and interest on which, when due and payable, without further investment or reinvestment, will provide sufficient moneys to pay when due the principal of and interest on such obligations, and (2) which securities described in clause (i) and (ii) are not available to satisfy any other claim, including any claim of such trustee or escrow agent or of any person claiming through such trustee or escrow agent or to whom such trustee or escrow agent may be obligated, including claims in the event of the insolvency of such trustee or escrow agent or proceedings arising out of such insolvency or (b) rated by either Standard & Poor's Ratings Service or Moody's Investors Service, or similar rating agency in its highest rating category (without regard to any refinement or gradation by numerical modifier or otherwise).

The initial investment of the Escrow Accounts will be designed to produce sufficient funds to provide fully for the payments of interest due on the Refunded Bonds from the closing of the Bonds to the respective earliest redemption dates. The Board reserves the right to modify the investments in the Escrow Accounts at any time and from time to time upon the condition that any reinvestments meet the sufficiency requirement in the preceding sentence. If the initial or any subsequent investment of the Escrow Accounts, or either of them, are solely in cash and/or Defeasance Obligations which are certified by an independent public accounting firm of national redemption to satisfy the sufficiency requirements stated above, the applicable series of the Refunded Bonds will be deemed to be defeased and no longer entitled to the benefit of the lien on the Severance Tax Bonding Fund revenues.

Sources and Uses of Funds

The following table sets forth the estimated sources and uses of funds to be available in connection with the sale of the Bonds.

SOURCES:	Series B-1 Bonds	Series B-2 Bonds
Par Amount	\$37,040,000.00	\$21,095,000.00
Reoffering Premium	2,616,357.10	1,708,502.55
Transfers from Prior Issue Debt Service Funds	960,500.00	551,500.00
Equity Contribution	<u>66,672.00</u>	<u>37,971.00</u>
TOTAL SOURCES	<u>\$40,683,529.10</u>	<u>\$23,392,973.55</u>
USES:		
Deposit to Escrow Accounts	\$40,453,175.98	\$23,227,409.21
Underwriters' Discount	143,210.93	81,540.61
Cost of Issuance	66,672.00	37,971.00
Gross Bond Insurance Premium	-0-	36,607.80
Contingency	<u>20,470.19</u>	<u>9,444.93</u>
TOTAL USES	<u>\$40,683,529.10</u>	<u>\$23,392,973.55</u>

SUMMARY OF REFUNDED BONDS

Series 2005B-1 Bonds

Severance Tax Bonds, Refunding Series 2001A

<u>Maturity</u> <u>July 1</u>	<u>Interest</u> <u>Rate</u>	<u>Principal</u> <u>Refunded</u>	<u>Redemption</u> <u>Date July 1</u>
2008	5.000%	\$5,985,000	2007
2009	5.000%	<u>1,665,000</u>	2007
		\$7,650,000	

Severance Tax Bonds, Series 2002A

<u>Maturity</u> <u>July 1</u>	<u>Interest</u> <u>Rate</u>	<u>Principal</u> <u>Refunded</u>	<u>Redemption</u> <u>Date July 1</u>
2009	5.000%	\$ 7,140,000	2007
2010	5.000%	7,495,000	2007
2011	5.000%	7,870,000	2007
2012	5.000%	<u>8,265,000</u>	2007
		\$30,770,000	

Series 2005B-2 Bonds

Supplemental Severance Tax Bonds, Series 2002A

<u>Maturity</u> <u>July 1</u>	<u>Interest</u> <u>Rate</u>	<u>Principal</u> <u>Refunded</u>	<u>Redemption</u> <u>Date July 1</u>
2009	5.000%	\$ 7,060,000	2007
2010	5.000%	7,345,000	2007
2011	5.000%	<u>7,655,000</u>	2007
		\$22,060,000	

If all of the Bonds of a maturity of a series of Refunded Bonds are not refunded and defeased, the Bond of that series and maturity to be advance refunded and defeased are to be selected by lot.

The accuracy of computations indicating that the respective amounts on deposit in the Escrow Accounts for the Refunded Bonds are sufficient to make the required payments in connection with the refunding of the Refunded Bonds will be verified by Causey Demgen & Moore Inc., Denver, Colorado, Certified Public Accountants & Consultants. See "VERIFICATION OF MATHEMATICAL CALCULATIONS".

SEVERANCE TAX BONDING FUND AND DEBT SERVICE REQUIREMENTS

Severance taxes have been collected by the State since the adoption of the Severance Tax Act in 1937. Since 1959, certain Severance Tax receipts and certain other moneys determined by the Legislature have been deposited into the Bonding Fund and used, in part, to retire bond issues which have funded a variety of capital improvements in the State.

Pursuant to the provisions of the Severance Tax Act and the Oil and Gas Severance Tax Act, severance tax receipts, including penalties and interest, and such other moneys as the Legislature in its sole discretion may from time to time determine (including interest earnings on moneys in the Bonding Fund and the project accounts and reversions from project accounts in the Bonding Fund), are deposited into the Bonding Fund. As of the date of this Official Statement no material amounts of other moneys (other than interest earnings) have been so deposited. The moneys in the Bonding Fund are pledged for the payment of principal of, premium, if any, and interest on Senior Severance Tax Bonds and Supplemental Severance Tax Bonds, and there are no other liens or encumbrances of any nature on or against (i) the Bonding Fund, or (ii) the net revenues derived from Severance Taxes which are required to be credited to the Bonding Fund.

Severance taxation is determined by State statute. The various Severance Tax rates and methods of their calculation are set forth hereinafter. See “SEVERANCE TAX REVENUE AND NATURAL RESOURCE PRODUCTION” below.

Investments

Funds on deposit in the Severance Tax Bonding Fund, including the Debt Service Account and the Project Fund (established according to the Bond Resolution), are invested by the State Treasurer at the direction and 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, and no such investment or deposit shall violate any applicable restrictions imposed by the Code (defined below) and 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 Resolution), interest earned on the amounts on deposit in the Debt Service Account shall be retained therein, and interest earned on amounts on deposit in the Project Fund shall be credited to the Debt Service Account and applied to the payment of principal of 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 investment was made.

Issuance of Severance Tax Bonds

The State Severance Tax Bonding Act authorizes the issuance and sale of Senior Severance Tax Bonds and Supplemental Severance Tax Bonds payable from the net receipts from taxes levied upon certain natural resource products severed and saved from the soil (“Severance Taxes”) in accordance with the provisions of, and as described in, the Act.

Severance Taxes are collected on a monthly basis by the New Mexico Department of Taxation and Revenue (the “Tax Department”) and deposited in the Tax Administration Suspense Account within the General Fund of the State. On or around the 25th day of the month following the collection of the Severance Taxes, those tax revenues are released from the Suspense Account and deposited in the Bonding Fund.

On December 31 and June 30 of each Fiscal Year, excess funds in the Bonding Fund are transferred into the Severance Tax Permanent Fund. Excess funds are defined as funds in excess of the next two semi-annual payments of debt service on Severance Tax Bonds and Supplemental Severance Tax Bonds. **Balances in the Severance Tax Permanent Fund are not pledged as Security for the Bonds.**

In addition to the sale of long-term Senior Severance Tax Bonds and Supplemental Severance Tax Bonds, the State issues short-term severance tax and supplemental severance tax funding notes from

time to time to utilize excess capacity available in the Bonding Fund, and to make those funds available for capital projects of the State. These short-term obligations generally have a maturity of five days or less, mature in the Fiscal Year in which they are issued and are purchased by the State Treasurer.

State Capital Program

Proceeds from Senior Severance Tax Bonds and Supplemental Severance Tax Bonds are an important source of capital financing for the State. Additional State sources of funding for capital projects are surplus general fund balances, general obligation bonds, highways bonds and bonds issued by the New Mexico Finance Authority. The following table summarizes capital authorization by funding source for Fiscal Year 2000 through Fiscal Year 2004 and Fiscal Year 2005 year to date through April 1, 2005.

Principal Sources of Capital Project Funding Fiscal Year Ending June 30 (Dollars in millions)

	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u> (as of May 15 Year to Date)
Proceeds from General Obligation Bonding						
Program						
General Obligation Bonds	-	\$62.6	-	\$130.9	-	\$111.9
General Obligation Funding Notes	-	-	-	-	-	-
Subtotal	<u>\$0.0</u>	<u>\$62.6</u>	<u>\$0.0</u>	<u>\$130.9</u>	<u>\$0.0</u>	<u>\$111.9</u>
Proceeds from Severance Tax Bonding Program						
Severance Tax Bonds ⁽¹⁾	\$59.7	-	\$67.0	\$73.9	\$71.0	-
Severance Tax Funding Notes ⁽²⁾	3.4	\$5.7	103.0	56.3	63.7	\$13.5
Supplemental Severance Tax Bonds	12.0	12.0	65.0	45.0	10.0	10.0
Supplemental Severance Tax Funding Notes ⁽²⁾	<u>55.00</u>	<u>74.5</u>	<u>35.1</u>	<u>111.8</u>	<u>151.8</u>	<u>106.7</u>
Subtotal	<u>\$130.1</u>	<u>\$92.2</u>	<u>\$270.1</u>	<u>\$287.0</u>	<u>\$296.5</u>	<u>\$130.2</u>
Proceeds From Other Sources						
General Fund	\$4.0	\$29.6	\$108.6	\$74.8	\$46.5	\$164.6
E-911 Revenue Bonds	-	4.5	-	-	-	-
Special Funds	11.5	20.8	15.0	6.9	26.5	42.0
Highway Bonds ⁽³⁾	690.6	198.8	162.8	16.0	700.0	-
New Mexico Finance Authority ⁽³⁾	<u>52.3</u>	<u>18.5</u>	<u>34.7</u>	<u>24.9</u>	<u>82.9</u>	<u>168.9</u>
Subtotal	<u>\$758.4</u>	<u>\$272.2</u>	<u>\$321.0</u>	<u>\$122.6</u>	<u>\$855.9</u>	<u>\$375.5</u>
Total	<u>\$888.5</u>	<u>\$426.9</u>	<u>\$591.1</u>	<u>\$540.5</u>	<u>\$1,152.4</u>	<u>\$617.5</u>

⁽¹⁾ The Board has authorized the sale of the Series 2005A Bonds expected to be delivered on June 15, 2005. Approximately \$85,605,000 of proceeds of the Series 2005A Bonds will be used for capital project funding.

⁽²⁾ The Board, in order to take advantage of Severance Tax 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.

⁽³⁾ 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.

Outstanding and Additional Senior Severance Tax Bonds

The Series 2005B-1 Bonds will be secured on a parity with the following Senior Severance Tax Bonds anticipated to be outstanding prior to the issuance of the Bonds (exclusive of those Senior Severance Tax Bonds additionally secured by escrowed securities). The Series 2005B-1 Bonds will be issued with a lien senior to the Supplemental Severance Tax Bonds anticipated to be outstanding prior to the delivery of the Bonds. See “Outstanding and Additional Supplemental Severance Tax Bonds” under this caption.

Principal Outstanding on Severance Tax Bonds Prior to the Delivery of the Bonds

Severance Tax Bonds, Series 2000	\$10,075,000
Severance Tax Bonds, Refunding Series 2001A	92,540,000
Severance Tax Bonds, Series 2002A	56,080,000
Severance Tax Bonds, Series 2003A	68,025,000
Severance Tax Bonds, Series 2004A	76,430,000
Severance Tax Bonds, Series 2005A ⁽¹⁾	<u>97,000,000</u>
Total	<u>\$400,150,000⁽²⁾</u>

(1) These Bonds are expected to be delivered on June 15, 2005.

(2) On July 1, 2005 the State will make regularly scheduled payments of \$62,646,375 and the total amount of outstanding Senior Severance Tax Bonds will be \$337,503,625.

Additional senior lien bonds may be issued in the future if all outstanding Senior Severance Tax Bonds, including the proposed bonds, can be serviced with not more than 50 percent of the annual deposits into the Bonding Fund as determined by the deposits during the Fiscal Year preceding the date of issuance of such Senior Severance Tax Bonds. Following the issuance of the Series 2005B-1 Bonds, Senior Severance Tax Bonds in the principal amount of approximately \$101,085,446* remain authorized but unissued, a portion of which are expected to be funded with the proceeds of Severance Tax Funding Notes to be issued by the end of June 2005.

Outstanding and Additional Supplemental Severance Tax Bonds

Supplemental Severance Tax Bonds were authorized pursuant to an amendment to the Act enacted in May 1999. Pursuant to 1999 and 2000 amendments to the Act, long-term Supplemental Severance Tax Bonds may be issued if all outstanding Severance Tax Bonds and Supplemental Severance Tax Bonds, including the proposed bonds, can be serviced with not more than 62.5 percent of the annual deposits into the Bonding Fund as determined by the deposits during the Fiscal Year preceding the date of issuance of such Supplemental Severance Tax Bonds. In addition, short-term supplemental severance tax funding notes may be issued in a Fiscal Year 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 Severance Tax Bonds and Supplemental Severance Tax Bonds and severance tax funding notes and supplemental severance tax funding notes does not exceed 95 percent of the deposits into the Bonding Fund. The Legislature had authorized \$600,000,000 of Supplemental Severance Tax Bonds (including short-term funding notes) for issuance by the Board from time to time after July 1, 1999. Effective April 5, 2001, as a result of an amendment made to the Act in the 2001 Regular Session of the Legislature and other previous legislation, the Legislature repealed the authority of the Board to issue the remaining authorized but unissued Supplemental Severance Tax Bonds and replaced it with authority to issue

* Preliminary, subject to change.

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.

The Series 2005B-2 Bonds will be secured on a parity with the following Supplemental Severance Tax Bonds anticipated to be outstanding prior to the delivery of the Bonds. The Series 2005B-2 Bonds will be issued with a lien subordinate to the Senior Severance Tax Bonds anticipated to be outstanding prior to the delivery of the Bonds. See “Outstanding and Additional Senior Severance Tax Bonds” under this caption.

**Principal Outstanding on
Supplemental Severance Tax Bonds
Prior to the Delivery of the Bonds**

Supplemental Severance Tax Bonds, Series 1999A	\$ 3,860,000
Supplemental Severance Tax Bonds, Series 2000C	5,750,000
Supplemental Severance Tax Bonds, Series 2002A	47,830,000
Supplemental Severance Tax Bonds, Series 2002B	37,665,000
Supplemental Severance Tax Bonds, Series 2003B	9,270,000
Supplemental Severance Tax Bonds, Series 2004B	<u>10,000,000</u>
Total	<u>\$114,375,000</u>

The following tables set forth actual and projected results for the Severance Tax Bonding Fund including receipts, disbursements, debt service requirements, transfers and projected debt service coverage ratios.

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Severance Tax Bonding Fund
Receipts, Disbursements and Transfers
Fiscal Year Ended June 30⁽¹⁾⁽²⁾⁽³⁾⁽⁴⁾
(Dollars in thousands)

	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Beginning Cash Balance	\$69,934	\$70,521	\$80,748	\$8,258	\$10,183
Receipts:					
Oil & Gas Severance Tax	156,146	309,364	206,552	218,410	287,320
Other Minerals Severance Taxes	<u>28,161</u>	<u>28,255</u>	<u>23,954</u>	<u>19,232</u>	<u>18,427</u>
Total Severance Taxes	\$184,307	\$337,620	\$230,506	\$237,643	\$305,594
Other Income:					
Interest on Investments	\$10,514	\$13,879	\$11,007	\$5,526	\$5,475
Bond Proceeds	827	100	-	-	-
Other financial sources	<u>1,114</u>	<u>4,662</u>	<u>4,533</u>	<u>13,988</u>	<u>8,268</u>
Subtotal	\$12,456	\$18,641	\$15,540	\$19,514	\$13,743
Total Receipts	\$196,763	\$356,261	\$246,046	\$257,157	\$319,337
Disbursements:					
Senior Bond Debt Service ⁽⁶⁾⁽⁷⁾⁽⁸⁾	\$69,924	\$68,227	\$132,511	\$71,425	\$67,596
Senior Short-term Obligations ⁽⁵⁾	3,400	5,685	103,078	54,026	63,653
Supplemental Bond Debt Service ⁽⁶⁾⁽⁷⁾⁽⁸⁾		2,101	14,947	17,569	18,216
Supplemental Short-term Obligations ⁽⁵⁾	54,954	74,500	35,075	111,752	151,857
Fiscal Charges	<u>421</u>	<u>367</u>	<u>890</u>	<u>459</u>	<u>618</u>
Total Disbursements	\$128,699	\$150,880	\$286,501	\$255,230	\$301,940
Transfers:					
To Severance Tax Permanent Fund	\$67,475	\$195,153	\$32,035	\$0	\$406
Other ⁽⁹⁾	<u>1</u>				
Total transfers	\$67,476	\$195,153	\$32,035	\$0	\$406
Ending Cash Balance, June 30	\$70,521	\$80,748	\$8,258 ⁽⁶⁾	\$10,183 ⁽⁷⁾	\$27,175 ⁽⁸⁾

(1) All receipts, expenditures and balances exclude amounts in rebate accounts received for potential arbitrate rebates.

(2) Balances exclude loan receivable from Department of Labor. Loan repayments amount are included as other income received. Fiscal Year 2000-01 loan repayments were \$192,918.

(3) Proceeds and expenditures attributable to refunding bonds are excludable from this table since these amounts are reserved for payment to the escrow agent and are not available for debt service payments.

(4) Columns may not total due to rounding.

(5) 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.

(6) Includes payment of \$71.5 million of debt service due 7/1/02 on senior and supplemental bonds that was paid on 6/29/02. Ending balance would have been \$79.8 million if this payment was not made during the period.

(7) Includes payment of \$77.4 million of debt service due 7/1/03 on senior and supplemental bonds that was paid on 6/19/03. Ending balance would have been \$87.6 million if this payment was not made during the period.

(8) Includes payment of \$77.43 million of debt service due 7/1/04 on senior and supplemental bonds that was paid on 6/29/04. Ending balance would have been \$104.5 million if this payment was not made during the period.

(9) Represents Fiscal Year 1999-2000 transfers to the escrow agent for cash defeasance of outstanding bonds.

Source: State Board of Finance based on the Comprehensive Financial Reporting Accounting System.

Severance Tax Bonding Fund Projected Receipts
Fiscal Year Ending June 30⁽¹⁾
(Dollars in thousands)

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Severance Tax Bonding Fund Receipts					
Natural Gas	\$243,848	\$222,839	\$213,717	\$204,754	\$195,950
Oil	\$91,728	\$82,162	\$77,059	\$72,051	\$71,330
CO2	\$900	\$900	\$900	\$900	\$900
Oil & Gas Advanced payments, etc.	<u>(\$1,047)</u>	<u>(\$0,593)</u>	<u>\$0,033</u>	<u>(\$2,111)</u>	<u>(\$1,244)</u>
Subtotal-Oil & Gas Severance Tax	\$335,429	\$305,308	\$291,709	\$275,594	\$266,936
Coal	\$17,062	\$16,550	\$16,054	\$15,572	\$15,105
Other Minerals	<u>\$1,000</u>	<u>\$1,000</u>	<u>\$1,000</u>	<u>\$1,000</u>	<u>\$1,000</u>
Subtotal-Other Severance Tax	\$18,062	\$17,550	\$17,054	\$16,572	\$16,105
Investment Earnings	\$9,000	\$9,000	\$9,000	\$9,000	\$9,000
Other Income	<u>\$300</u>	<u>\$300</u>	<u>\$300</u>	<u>\$300</u>	<u>\$300</u>
Total Receipts	\$362,791	\$332,158	\$318,062	\$301,466	\$292,341
Scheduled Senior Debt Service⁽²⁾	\$68,204	\$70,863	\$69,700	\$61,891	\$59,767
Senior Bond Debt Service Coverage	5.32x	4.69x	4.56x	4.87x	4.89x
Scheduled Supplemental Debt Service⁽²⁾	\$19,008	\$20,243	\$20,119	\$18,020	\$15,899
Supplemental Bond Debt Service Coverage	4.16x	3.65x	3.54x	3.77x	3.86x

⁽¹⁾ Columns may not total due to rounding.

⁽²⁾ Includes debt service on the Bonds and gives effect to the issuance of the Series 2005A Bonds. Excludes debt service on advance 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.

Source: NM Department of Finance and Administration and Fiscal Strategies Group.

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**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⁽¹⁾	Projected Senior Coverage	Scheduled Supplemental Debt Service⁽¹⁾	Projected Supplemental Coverage
2005	\$362,790,684	\$ 68,204,432	5.32x	\$19,007,653	4.16x
2006	332,158,195	70,863,315	4.69x	20,242,763	3.65x
2007	318,062,167	69,700,350	4.56x	20,118,842	3.54x
2008	301,465,787	61,891,013	4.87x	18,020,276	3.77x
2009	292,340,784	59,766,738	4.89x	15,899,233	3.86x
2010	212,040,869	42,423,400	5.00x	15,598,983	3.65x
2011	209,799,263	36,144,656	5.80x	15,589,920	4.06x
2012	207,975,106	36,294,050	5.73x	15,568,239	4.01x
2013	204,587,342	36,490,900	5.61x	8,122,849	4.59x
2014	202,393,157	28,616,738	7.07x	2,463,283	6.51x
2015	200,815,103	19,438,725	10.33x	1,178,750	9.74x

⁽¹⁾ Includes debt service on the Bonds. Excludes debt service on advance 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.

Source: NM Department of Finance and Administration and Fiscal Strategies Group.

SEVERANCE TAX REVENUE

The minerals extracted from the State that contribute the largest portion of Severance Tax revenues are natural gas, oil and coal. Severance Tax collections on these three mineral resources produced 99.8 percent of total Fiscal Year 2004 Severance Tax Bonding Fund tax collections. Severance Taxes from natural gas and oil together represent approximately 94.02 percent of total Fiscal Year 2004 Bonding Fund tax receipts.

The State's Energy, Minerals, and Natural Resources Department ("EMNRD") records and generates data on mineral resources in the State. EMNRD produces annual reports on the State's mineral resources. The Tax Department compiles reports of taxable volume, value, deductions and tax receipts by commodity and land type. Annual production estimates and projections of Severance Tax receipts are made by the Department of Finance and Administration (DFA) in cooperation with the Tax Department. See "APPENDIX C: FORM OF ATTORNEY GENERAL'S NO LITIGATION LETTER" for a discussion of pending litigation and other proceedings concerning the collection of Severance Taxes.

Severance Tax Collections and Reporting

Operators, purchasers or working interest owners are required to submit monthly reports to the Tax Department showing the total value, volume and kind of products sold from each production unit during the 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" a designation for a well or group of wells that is assigned by the Tax Department 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 counties, school districts and municipalities. The Tax Department receives approximately 750 oil and gas returns per month.

These returns contain an average of about 75,000 lines of detailed information about production from different production units.

Complete reporting forms must be mailed or delivered, or their information electronically transmitted, on or before the twenty-fifth day of the second month after the calendar month for which the report is required. Taxpayers whose total tax liability for the month (including the oil and gas emergency school tax, the oil and gas conservation tax and the oil and gas ad valorem tax, as well as the oil and gas severance tax) exceeds \$25,000 must provide payment by automated clearinghouse or by wire transfer on or before the due date. Taxpayers who fail to report or pay in a timely fashion are assessed interest at a rate of 1.25 percent per month beginning the day after the due date and continuing until the date the tax is reported or paid. A penalty is assessed when a taxpayer fails to pay any tax or file any report by the due date because of negligence or disregard of rules and regulations. A penalty is charged at a rate of 2 percent a month, up to a maximum of 10 percent of the tax due.

The State maintains an automated database system (“ONGARD” for Oil and Natural Gas Administration and Revenue Database) to monitor transactions with 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 tax amounts received by the Tax Department are deposited into the Oil and Gas Suspense Fund. Using the ONGARD system, the Tax 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, once a month, to the Bonding Fund.

Severance Tax on Indian Land

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

The Tax Department reports that natural gas production and crude oil production on Indian land were approximately 4.0 percent and 1.0 percent, respectively, of total taxable statewide production in Fiscal Year 2004. DFA estimates that oil and gas production on Indian lands generated \$8.3 million in Severance Tax revenues to the State in the production months corresponding to Fiscal Year 2004. The Tax Department estimates that coal production on Indian land ranges from 40-45 percent of total statewide production from year to year. No potash or copper is produced on Indian land.

Laws 1995, Chapter 171, authorizes an intergovernmental tax credit against State production and property taxes for similar taxes imposed by tribal governments. The tax 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 are raised after March 1, 1995, then the amount of the State’s credit would be lowered. The Tax Department estimates that total credits claimed under this provision were about \$1.7 million in 2004. About \$0.8 million of these credits were applied against oil and gas

severance tax liability. The Bonding Fund revenue projection assumes that this amount will grow slowly in the future.

Laws 2001, Chapter 134, provides 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 Severance Tax Bonding Fund revenue by \$3.7 million in Fiscal Year 2004. Laws 2002, Chapter 15, created the Jicarilla Apache Tribal Capital Improvement Tax Credit. This new 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 does not apply against the severance tax revenues due on the same production, and therefore does not affect revenue pledged to the Bonds.

NATURAL GAS PRODUCTION AND SEVERANCE TAX REVENUE

Natural Gas Reserves and Well Completions

The chart on the following page presents the U.S. Energy Information Administration (“EIA”) estimates of natural gas “proved reserves” in New Mexico over the years 1984 to 2003. Proved reserves are estimates of recoverable volumes under existing economic and operating conditions. They represent the narrowest measurement of energy resources. Each year the EIA updates its estimates to reflect new information, new discoveries and the production during the year. Increases due to revisions and new discoveries usually offset some or all of the decline due to current production.

New Mexico’s proved natural gas reserves were estimated to be 18,226 billion cubic feet (bcf) at the end of calendar year 2003, down from 18,597 bcf at the end of calendar year 1993, a decade earlier. Reserves declined by about 371 bcf during the ten year period although production was about 15,975 bcf. Additions through new discoveries and revised estimates have offset 97.7 percent of the production during the decade. The current reserve estimate represents a New Mexico reserve-to-current-production ratio of 11.94.

New Mexico’s proved natural gas reserves increased in the early 1990’s due to exploration and development in coal seams that was triggered by the federal income tax credit (Section 29 of the Internal Revenue Code). The credit is currently worth more than \$1.00 per thousand cubic feet (mcf) of production and grows with inflation. The credit is no longer available for production occurring after 2002. Production from coal seam formations now accounts for approximately one-third of total statewide natural gas production.

The “proved reserves-to-production” ratio is a measure analogous to inventory-to-production for manufacturers. It represents the known resources that could be developed at today’s prices. As is the case for other industries, oil and gas producers have to balance their need for adequate inventories with the cost of exploring and developing the reserves. Although they have maintained higher ratios at times in the past, the industry has targeted lower ratios in recent years as a cost savings measure.

Over the last two decades, gas producers have replaced most of their production with new discoveries. As a result, reserves of natural gas at the end of calendar year 2003 were 1,678 bcf above the level at the beginning of 1984, although 25,706 bcf had been produced in the period. Replacement of reserves by new discoveries and further development of existing formations is a key component of the State’s long-term production forecast. New discoveries are expected to offset much of future production. As a result, annual production is expected to decline only gradually. Over time, technology has advanced the discovery of new reserves and the production capability for reserves. The reserves to current production ratio has stabilized between ten and twelve over the last eight years.

New Mexico Natural Gas⁽¹⁾ Reserves
(Gas numbers in billion cubic feet)

<u>Year</u>	<u>Beginning Reserves</u>	<u>Net Additions/ Adjustments</u>	<u>Estimated Production</u>	<u>Ending Reserves</u>
1984	16,548	444	947	16,045
1985	16,045	290	893	15,442
1986	15,442	581	692	15,331
1987	15,331	552	813	15,070
1988	15,070	4,194	781	18,483
1989	18,483	1,433	860	19,056
1990	19,056	1,723	965	19,814
1991	19,814	1,053	1,109	19,758
1992	19,758	1,889	1,248	20,399
1993	20,399	-379	1,423	18,597
1994	18,597	-1	1,489	17,107
1995	17,107	1,660	1,625	17,142
1996	17,142	915	1,572	16,485
1997	16,485	1,512	1,592	16,405
1998	16,405	1,473	1,619	16,259
1999	16,259	2,137	1,646	16,750
2000	16,750	3,382	1,623	18,509
2001	18,509	1,699	1,649	18,559
2002	18,559	1,528	1,634	18,453
2003	18,453	1,299	1,526	18,226

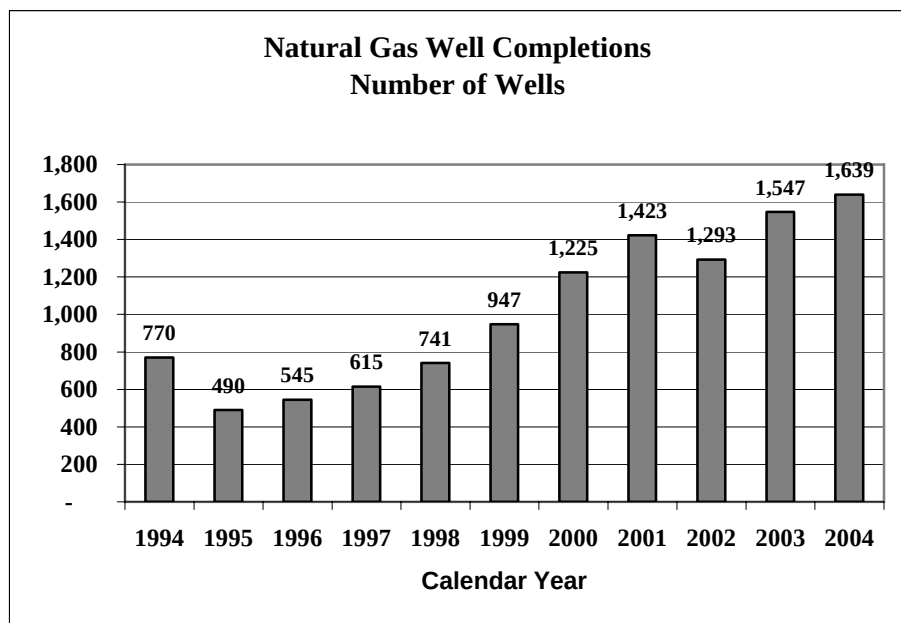
⁽¹⁾ Wet, after lease separation. Wet after lease separation represents the volume of natural gas that is marketable after exclusion of pentanes, hydrocarbons and nonhydrocarbons. The presence of these chemicals renders gas unmarketable.

Source: EIA

Drilling activity in New Mexico has subsided somewhat following a boom in 1990 and 1991 that was stimulated by the deadline for the federal coal seam tax credit. The collapse of oil prices in 1998 caused sharp cutbacks in drilling for both oil and gas wells. The subsequent recovery of prices for both oil and gas has spurred a sharp increase in drilling activity. The drilling rig count in the State has more than tripled since 1995 in response to higher oil and natural gas prices.

In early August 1999, a joint venture between Sonat Raton and PennzEnergy Corporation announced plans for an extensive development program in the Raton Basin in northeastern New Mexico. Since 2000, production from the Raton Basin has yielded 39.7 million mcf. Production in Fiscal Year 2004 was 16.6 million mcf. Natural gas prices from production in the Raton Basin are higher than natural gas prices from production in the San Juan Basin because the Raton Basin has better pipeline access to potential markets.

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Source: NM Energy, Minerals and Natural Resources Department.

Natural Gas Markets

Since 1986, total U.S. consumption of natural gas has grown in all but one year, with a compound annual average growth rate of 2.4 percent, reaching 22.3 trillion cubic feet (tcf) in calendar year 2003. Consumption increases have been driven by the expanding economy and by environmental concerns with coal-fired power generation, as well as by relatively low gas prices. During the same period, according to the EIA, domestic production has also increased steadily, but more slowly, from less than 17 tcf in 1986 to 19.7 tcf in calendar year 2001, a compound growth rate of about 1 percent. Declining production in mature provinces such as West Texas has been offset by sharp production increases from coal-bed methane formations and deepwater Gulf of Mexico deposits. The growing gap between domestic production and domestic consumption has been met by sharply growing imports, from 1.1 tcf in 1986 to 4.0 tcf in calendar year 2001.

The balance between supply and demand has shifted periodically during the 1990's, depending on the availability of pipeline capacity for expanded imports, as well as the usual weather-related conditions. Average wellhead prices were relatively stable from 1988 through 1992, but have fluctuated since 1993. New Mexico producers have generally received a lower price at the wellhead due to the longer distance from the dominant east coast markets than the competing product from Texas and Louisiana, and the resulting higher transportation costs. This price differential was reversed in 2000 during the power generation crisis in California, and New Mexico's proximity to that market. National average wellhead prices and average New Mexico wellhead prices for 1995 through 2004 are presented in the following table.

**Average Wellhead Price by Calendar year
(\$ per thousand cubic feet)**

	<u>1995</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
National Average Wellhead Price	\$1.55	\$2.17	\$2.32	\$1.96	\$2.19	\$3.68	\$4.00	\$2.95	\$4.88	\$5.49
New Mexico Producers	\$1.26	\$1.67	\$1.76	\$1.76	\$2.11	\$3.43	\$3.89	\$2.68	\$3.60	\$4.68
NM as a % of National Average	81%	77%	76%	90%	96%	93%	97%	91%	74%	85%

Source: National average prices: EIA, "Monthly natural gas prices" selected issues. New Mexico average prices: DFA calculations based on severance tax return data.

New Mexico's producers have benefited from higher wellhead prices since 1996. Economic growth in California, the end-use market for a majority of gas produced in the State, has caused prices received in the San Juan basin to increase relative to eastern markets. Additions to pipeline infrastructure have enabled the State's producers to move gas east or west to the more profitable market. The result has been improved New Mexico wellhead prices compared to the national average.

Natural Gas Production

Total natural gas production in New Mexico increased sharply in the early 1990's due to increased coal seam production in the San Juan Basin. This production was stimulated by federal income tax credits that expired at the end of calendar year 2002. Coal seam gas production now accounts for approximately one-third of total statewide production. Total statewide production fell below 1,600 bcf in Fiscal Years 2003 and 2004. Total revenue doubled in Fiscal Year 2001 as shortages caused gas prices to spike to unprecedented levels during the winter of 2000-2001. Taxable production volume, sales revenue and average price per thousand cubic feet for Fiscal Years 1995 through 2004 are presented in the following table.

**Natural Gas Subject to Taxation
Production, Revenues and Average Price
Fiscal Years 1995-2004**

	<u>1995</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Sales Volume (bcf)	1,465	1,509	1,543	1,609	1,615	1,625	1,628	1,616	1,570	1,534
Sales Revenues (millions)	\$2,124	\$2,101	\$3,290	\$3,343	\$2,722	\$3,149	\$6,680	\$3,391	\$4,493	\$5,887
Average Price per mcf	\$1.45	\$1.39	\$2.13	\$2.08	\$1.69	\$1.94	\$4.10	\$2.10	\$2.86	\$3.84

Source: NM Department of Finance and Administration.

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The following table sets forth the production levels of the State's largest gas producers in calendar year 2003.

Ten Largest Natural Gas Producers in New Mexico and 2003 Production

	<u>Billion Cubic Feet</u>
Burlington Resources	386
Conoco Phillips Company	226
BP America Production Co.	121
Devon Energy Production Co.	113
Yates Petroleum	75
Marathon Oil Company	62
Chevron USA Inc.	48
Williams Production Co.	41
XTO Energy Inc.	38
Energen Resources Corp.	34

Source: NM Energy, Minerals and Natural Resources Department, Oil Conservation Division.

Severance Taxes on Natural Gas

Severance taxes are levied by statute on the sale or transport out of state of natural gas produced in the State. State taxation of minerals production for the general fund began as early as 1933. The Severance Tax Bonding Act, enacted in 1961, earmarked a portion of the existing severance tax to pay debt service on severance tax bonds, with remaining revenues going to the general fund. The severance tax at that time was 2.5 percent of the marketable sales value, with deductions allowed for royalties to governments and for certain processing and transportation expenses. Beginning in 1973, the Severance Tax Permanent Fund was created, receiving excess severance tax revenues not required for debt service payments.

The tax rate was increased to 3.75 percent of value in 1974. Beginning in 1977, the tax rate was converted to a per unit basis, \$0.05 per mcf of gas, with a deduction allowed for royalties to governments. A surtax was added, equal to the base tax rate times the percentage increase in the Consumer Price Index (CPI) from the base year. This surtax rate was updated annually. The base tax rate was increased to \$0.087 per mcf in 1980, and the surtax provision continued to apply.

By July 1, 1986 the surtax had reached \$0.076 and the total tax rate was \$0.163 per mcf. With the sharp decline in wellhead natural gas prices in 1986, the effective severance tax rate was over 8.0 percent of gross sales value. The combined effective tax rate on gas production, including general fund taxes, was over 11.0 percent, significantly higher than in neighboring gas-producing states. The 1987 Legislature responded to declining prices by converting the tax to 3.75 percent of value on a phased in basis. Beginning July 1, 1990, the new tax rate applied to all production.

The 1995 Legislature authorized reduced severance tax rates for certain categories of production. A 10-year exemption from Severance Taxes was provided for production from previously non-producing wells ("restoration"). A 50 percent rate reduction was provided for incremental production from a qualifying work over project ("recompletion"). Qualified volumes are expected to grow slowly over time.

In response to sharply lower oil prices and declining production of oil and associated natural gas, the 1999 Legislature adopted new severance tax incentives for production from recompletion wells and stripper wells. Instead of a 50 percent rate reduction (from 3.75 percent to 1.875 percent) for only the *incremental* production from recompletion wells, a tax rate of 2.45 percent was applied to all production

from qualified wells. This provision had a minimal effect on severance tax collections, as the higher incentive tax rate offsets the increase in eligible volumes.

For stripper well production, the 1999 legislation introduced a sliding scale of applicable tax rates, depending on the prevailing taxable value of products. For natural gas, a stripper well is defined as one having average daily production of less than 60,000 cubic feet per day. For oil wells, the threshold is 10 barrels per day.

The following table summarizes incentive tax rates applied to various categories of oil and gas production in New Mexico as of Fiscal Year 2004. However, due to the rise in oil and gas prices, most of these incentive programs are not currently in effect. Should prices decline in the future, some of these incentives will be again be applicable.

Oil and Gas Tax Incentive Programs

<u>Incentive Category</u>	<u>Incentive Tax Rate</u>	<u>Threshold price below which incentive rate applies</u>	<u>Qualified production as a percent of Fiscal Year 2004 total</u>
Restoration wells	0.0%	\$24.00 per barrel ⁽¹⁾	0.0% Natural Gas ⁽³⁾ 0.0% Oil ⁽³⁾
Recompletion wells	2.45%	\$24.00 per barrel ⁽¹⁾	0.0% Natural Gas ⁽³⁾ 0.0% Oil ⁽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

⁽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 Fiscal Year 2004 because average taxable value exceeds the threshold levels.

Source: NM Department of Finance and Administration.

Projections of Severance Tax Revenues from Natural Gas

Natural gas production in the State is expected to decline by an average 1 percent to 2 percent per year in the future. Most of the wells in the State have been producing for a prolonged period, and the loss of pressure in gas formations will lead to declines in per well production that will be partially offset by new drilling. New gas development in the Raton Basin could result in an increase in future gas production in the State.

The price outlook is based on analysis of national markets by the Cambridge Energy Research Associates (CERA). Natural gas prices rose to unprecedented levels during the winter of 2000-2001 as supplies failed to keep up with increasing demand and inventories reached record low levels. After falling back to lower levels, in response to the economic recession and continued slow economic growth, prices rose again in anticipation of the war with Iraq. Notwithstanding volatility in prices over the past

several years, CERA expects the demand for gas to continue to grow and prices to remain stable at current levels.

Almost all new power plant capacity being planned at the present time is gas-fired. Environmental concerns with coal power make gas a preferred option. In addition, deregulation of electric power markets places a premium on “distributed generation” – power generation facilities that are closer to end use markets than traditional, central-station facilities. Under likely scenarios, CERA sees the potential for natural gas demand to increase by 50 percent over the next 10 to 15 years. Given relatively limited options for domestic supply, and even assuming increases in imports, the result should be strong upward pressure on natural gas prices in the long term.

The average price received by New Mexico producers increased from \$2.46 in Fiscal Year 2000 to \$4.98 in Fiscal Year 2001. Prices decreased in Fiscal Year 2002 to \$2.60, increased in Fiscal Year 2003 to \$3.60 and increased in Fiscal Year 2004 to \$4.60. Based on the long-term outlook for natural gas demand projected by CERA, the price received by New Mexico producers is expected to approximate \$5.70 in Fiscal Year 2005 and decline to \$4.80 by Fiscal Year 2006.

The severance tax base for natural gas is defined as the wellhead value less deductions for the expense of transporting and processing their product to the first point of sale. In addition, deductions are allowed for royalties paid to governmental entities (federal, state and tribal). The combined value of all deductions has averaged about 20 percent of gross wellhead sales value in recent years. Thus, estimated taxable value is about 20 percent lower than the sales prices reported in the following table.

**New Mexico Gas Volume, Price and Severance Tax Projections
Fiscal Years Ending June 30**

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Natural gas sales (bcf)	1,525	1,510	1,495	1,480	1,465
Average sales price (\$/mcf)	\$5.20	\$4.80	\$4.65	\$4.50	\$4.35
Severance Taxes on Gas (in thousands)	\$243,848	\$222,839	\$213,717	\$204,754	\$195,950

OIL PRODUCTION AND SEVERANCE TAX REVENUE

Oil Reserves and Production

The chart below presents the EIA’s estimate of oil “proven reserves” from 1984 to 2003. Proven reserves are estimates of recoverable barrels under existing economic and operating conditions. As oil prices rise, proven reserves increase. They represent the narrowest measurement of the country’s energy resources. Each year the EIA updates its estimates to reflect new information, new discoveries and production during the year. Increases due to revisions and new discoveries usually offset some or all of the decline due to current production. The EIA reports on proven reserves of crude oil in the State on the basis of company surveys. Current New Mexico reserves represent approximately 11.1 years of production.

The “proven reserves-to-production” ratio is a measure analogous to inventory-to-production for manufacturers. It represents the known resources that could be developed at today’s prices. As is the case for other industries, oil producers have to balance their need for adequate inventories with the cost of exploring and developing the reserves. Although they have maintained higher ratios at times in the past, the industry has targeted lower ratios in recent years as a cost savings measure.

Over the last two decades, oil producers have replaced most of their production with new discoveries. Oil reserves were only 180 million barrels lower at the end of calendar year 2003 than at the beginning of calendar year 1984 although production during the same period was 1,341 million barrels. During this period, 86.6 percent of production was replaced by new discoveries and developments during the period. Replacement of reserves by new discoveries and further development of existing formations is a key component of the State's long-term production forecast. New discoveries are expected to offset much of future production and annual production is expected to decline gradually.

New Mexico Oil Reserves
Crude Oil⁽¹⁾

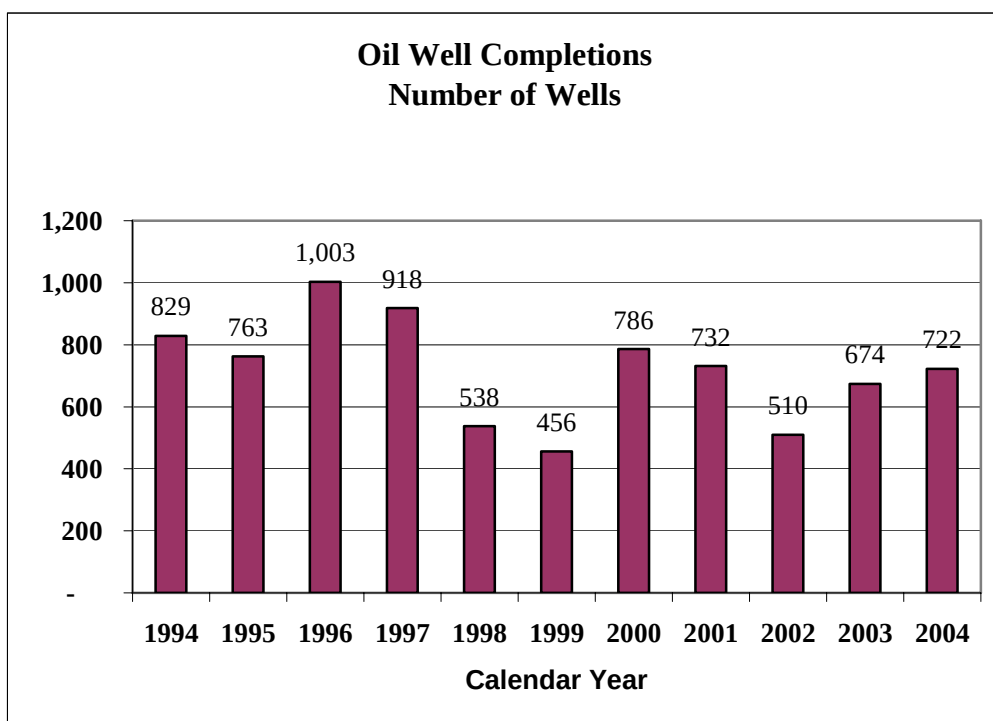
<u>Year</u>	<u>Beginning Reserves</u>	<u>Additions/ Adjustments</u>	<u>Estimated Production</u>	<u>Ending Reserves</u>
1984	857	156	76	937
1985	937	104	75	966
1986	966	26	73	919
1987	919	79	69	929
1988	929	66	68	927
1989	927	68	65	930
1990	930	83	64	949
1991	949	99	65	983
1992	983	103	67	1,019
1993	1,019	14	64	969
1994	969	-189	66	714
1995	714	82	71	725
1996	725	93	74	744
1997	744	64	73	735
1998	735	-47	68	620
1999	620	159	61	718
2000	718	58	57	719
2001	719	58	62	715
2002	715	59	64	710
2003	710	26	59	677

⁽¹⁾ Barrels in millions.

Source: U.S. Energy Information Administration.

Potential new development of oil resources is indicated by exploration and drilling activity. Secondary or tertiary recovery projects (water or carbon dioxide injection) typically require new development wells. The following chart presents oil well completions during the period 1994 through 2004.

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Source: NM Energy, Minerals and Natural Resources Department.

Oil Production

Oil production in the State reached its highest level in 1969 at 129.2 million barrels. After declining during the 1980's, a period of dramatically lower oil prices, production had stabilized around 70 million barrels per year during most of the 1990's. Application of three-dimensional seismic technology has been very successful in New Mexico, enabling production from shallower depths in older, mature fields. The following table sets forth the production levels of the largest oil producers in the State in calendar year 2003.

Ten Largest Oil Producers in New Mexico and 2003 Production Millions of Barrels

	<u>Millions of barrels</u>
Chevron USA. Inc.	7.5
Conoco Phillips Company	4.5
Devon Energy Production Co.	4.0
Yates Petroleum Corp.	3.7
Marbob Energy	3.5
Marathon Oil Co.	3.1
Occidental Permian	2.7
Mack Energy Corp.	2.6
Pogo Production Co.	2.0
Amerada Hess Corp.	1.8

Source: NM Energy, Minerals and Natural Resources Department, Oil Conservation Division.

Severance Taxes are levied on oil on the basis of sales value at the time of either sale or transportation from the State. Oil production and oil sales are related but are not directly proportional

because of stockpiling and price fluctuations from period to period. Estimates of oil sales occurring in the last ten Fiscal Years are presented in the following table.

	Oil Subject to Taxation Production, Revenues and Average Price <u>Fiscal Years 1995-2004</u>									
	<u>1995</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Sales Volume (bbls in millions)	69.5	75.7	75.4	73.5	66.0	67.3	70.3	69.0	68.5	66.5
Sales Revenues (billions)	\$1.123	\$1.300	\$1.590	\$1.238	\$0.740	\$1.485	\$2.018	\$1.521	\$1.904	\$2.126
Average Price per Barrel	\$16.16	\$17.17	\$21.37	\$16.84	\$11.22	\$22.07	\$28.71	\$22.04	\$27.80	\$31.97

Source: NM Department of Finance and Administration.

Severance Taxes on Oil

Severance taxes are levied by statute on the sale or transport out of state of oil produced in the State. The severance tax rate on oil was increased to 3.75 percent of sales value in 1974. Beginning in 1977, the rate was converted to \$0.45 per barrel, with a surtax indexed to the CPI. In 1980, the tax rate was converted back to 3.75 percent of value.

In 1992, the Legislature provided a 50 percent reduction of the severance tax rate applied to oil produced through enhanced recovery methods. Enhanced methods include carbon dioxide miscible fluid displacement, water flood, pressure maintenance and thermal methods. The reduced rate applies to all production from an enhanced recovery project following certification of a positive production response by EMNRD's Oil Conservation Division.

The 1995 Legislature authorized reduced severance tax rates for certain categories of production. A 10-year exemption from Severance Tax was provided for production from previously non-producing wells ("restoration"). A 50 percent rate reduction was provided for incremental production from a qualifying work over project ("recompletion"). During Fiscal Year 1999, 100,000 barrels of oil had qualified for the restoration tax exemption. During the same period, 500,000 barrels of oil had qualified for the recompletion rate reduction. Combined, these volumes represent less than 1.0 percent of annual production of oil. Qualified volumes are expected to grow slowly over time. The 1999 Legislature expanded the incentive program for recompletion wells and created a new incentive for stripper wells.

Projections of Severance Tax Revenues from Oil

Volume of production: The natural rate of production decline from an oil field, absent application of enhanced recovery methods ("EOR") or additional drilling for exploration and development, is usually estimated at 10 percent per year. During most of the 1990's, producers prevented a decline in total production by a combination of new well drilling, well maintenance activity and EOR investment. Oil producers responded to higher world oil prices by increasing output in Fiscal Year 2001. Since then, output has declined by 1 percent to 2 percent and is expected to continue at this rate.

Prices: Average annual oil prices received by New Mexico producers have fluctuated from a low of \$11.75 to a high of \$31.97 over the past decade. A dramatic cycle in crude oil prices was initiated in the fall of 1997, when the OPEC cartel announced its intention to increase production quotas. Coincident with a worldwide economic slowdown, the announcement led to a drop of about 50 percent in world crude oil prices. A new agreement to reduce production levels was reached by the cartel during the spring of 1999. Since that time, the OPEC action and the dramatic rise in the domestic price for natural gas led

to a spike in oil prices in 2001. Since that time, prices abated as world economic growth slowed, and then rose again in anticipation of potential production shortfalls related to the war in Iraq. A long-term downward trend in both pricing and production levels is expected, as set forth in the table below. For New Mexico producers, a price of \$42.00 is expected for Fiscal Year 2005 and is expected to decline to \$38.00 beginning in Fiscal Year 2006 and to \$25.00 beginning in Fiscal Year 2010 and the rest of the forecast period.

**New Mexico Oil Volume, Price, and Severance Tax Projections
Fiscal Years Ending June 30**

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Oil sales (million barrels)	64.0	63.4	62.7	62.1	61.5
Average price (\$/barrel)	\$42.00	\$38.00	\$36.00	\$34.00	\$34.00
Severance Taxes on Oil (in thousands)	\$91,728	\$82,162	\$77,059	\$72,051	\$71,330

Source: NM Department of Finance and Administration.

COAL PRODUCTION AND SEVERANCE TAX REVENUE

Coal Reserves and Production

Coal mining is currently based in the San Juan Basin in the northern and northwestern regions of the State, which accounts for all of the State's coal production. The State Institute of Mining and Technology, Bureau of Mines and Mineral Resources ("IMT") estimates that approximately 11 billion tons of strippable resources and approximately 28.4 billion tons of deep resources exist as reserves in the San Juan Basin. Total economically recoverable coal resources in the State are reported at approximately 45.8 billion tons. These estimates have been revised downward substantially since 1994 as a result of a thorough review of reserves by IMT. The quality of coal located in the State ranges from high-heat content bituminous coal to lower rank sub-bituminous coal. Coal found in the State is generally low in sulfur content, with wide variations in ash and moisture content.

The demand for coal is largely a derived demand, depending heavily on the electrical power market. The power market in the western U.S., in turn, depends heavily upon economic conditions in California and upon regulatory actions taken in that market. The forecast assumes no resurrection of an earlier proposal to impose environmental penalties in California on the use of electricity from coal-fired power plants. Such penalties would likely affect the level of sales of New Mexico coal.

Wholesale electricity prices in the western U.S. increased to unprecedented levels during the winter of 2000-2001. New generating capacity had not kept pace with increasing demand over the latter part of the 1990s, leading to reserve margins that fell below 10 percent. In addition, natural gas prices rose to unprecedented levels, which dramatically increased the cost of marginal electricity supplies. Wholesale prices remained high through the early spring, but fell back into their historical range in the summer of 2001 as the slowing economy and mild weather reduced demand. Natural gas prices have fallen by more than 50 percent, reducing fuel costs for electricity generators.

Total coal sales are expected to decline gradually in the forecast due to increased competition and environmental concerns. An increasing portion of total sales is expected to be eligible for the surtax exemption.

Severance Taxes on Coal

Severance taxes have been levied on coal production in New Mexico since 1937. Revenues were distributed to the State general fund until adoption of the Severance Tax Bonding Act in 1961. Tax rates were imposed on an ad valorem basis, 0.125 percent of value from 1937 to 1974, and 0.5 percent of value from 1974 to 1977. In 1977, rates were converted to \$0.38 per ton plus a surtax indexed to the CPI. The base rate was then increased to the current base rate of \$0.57 per ton in 1980. A slightly reduced base rate of \$0.55 per ton was provided enacted for underground-mined coal in 1982. The current surtax rate is \$0.61 per ton, and \$0.59 for underground-mined coal, resulting in current combined rates for coal subject to severance surtax of \$1.18 for surface-mined coal and \$1.14 for underground-mined coal.

Effective July 1, 1989, the severance surtax was frozen for a period of four years at \$0.60 per ton for surface coal and \$0.58 per ton for underground coal. When added to the base tax rate, this action had the effect of freezing the total rate at \$1.17 per ton for surface coal and \$1.13 per ton for underground coal (only a very small portion of coal production comes from underground mines). Originally the surtax freeze was to have terminated on July 1, 1993. However, the 1993 Legislature extended the freeze until July 1, 1994, after which time the surtax is adjusted in accordance with the increase in the Producer Price Index (“PPI”) for coal. The surtax formula provides that in no case will the surtax be decreased, so a fall in the PPI for coal will not trigger a drop in the surtax rate. The surtax rate for Fiscal Year 1995 increased \$0.01 to \$0.61 per ton for surface coal and \$0.59 per ton for underground coal. The surtax rate for Fiscal Year 2006 will be \$0.69 per ton for surface coal and \$0.67 per ton for underground coal.

The 1990 Legislature suspended the surtax until July 1, 2009, for coal sold under new contracts entered into on or after July 1, 1990, and before July 1, 1994. The provision also extends to incremental sales under existing contracts measured by the increase in sales over the annual average established in Fiscal Years 1987-1989. The 1992 Legislature extended the surtax exemption to incremental sales under renegotiated contracts. Subsequent Legislatures extended the period for new contracts to qualify for the extension to June 30, 1999.

The 1999 Legislature reexamined coal severance taxes in the light of deregulation of the electric power market. Increased competition in power markets makes it harder for utilities to pass on the cost of high production taxes on coal used in generation. A study of New Mexico’s coal taxes by economists at the Tax Department and the DFA indicated that New Mexico’s taxes were among the highest in the region.⁽¹⁾ In view of these facts, the 1999 Legislature and Governor acted to repeal the sunset of the severance surtax exemption. Thus, as existing contracts expire which are currently subject to the surtax, any subsequent contracts will be exempt from the surtax. Although a total of \$9.7 million in severance surtax was collected in Fiscal Year 2004, the impacts of the new statute are expected to be small, as most contracts subject to the surtax do not expire for a number of years. The full impact of the provision will not be felt until all existing contracts expire, in about 13 years.

The table below sets forth data on coal production, pricing and average tax rates for the past five Fiscal Years.

(1) “Taxation of Coal Production in Western States,” by Kelly O’Donnell, N.M. Taxation and Revenue Department and Dr. Thomas Clifford, N.M. Department of Finance and Administration, presentation to the Revenue Stabilization and Tax Policy Committee, November, 1988.

Coal Production, Pricing and Tax Rates
Fiscal Years 2000-2004

	Fiscal Year Ending June 30				
	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Total Sales Volume (short tons)	\$ 27,259,907	\$ 27,131,704	\$ 26,589,634	\$ 26,704,979	\$ 25,584,920
Surface Mined Surtax Exempt Volume	9,293,451	10,318,045	10,405,420	10,918,338	10,104,895
Surface Mined Non-Exempt Volume	17,960,718	15,705,560	14,715,458	13,626,804	14,066,790
Underground Non-Exempt Volume	5,738	1,108,099	1,468,656	2,159,837	1,512,643
Total Sales Revenue	\$567,067,376	\$548,233,652	\$528,324,790	\$611,561,557	\$583,588,317
Average Price Per Ton	\$21	\$20	\$20	\$22	\$23
Total Intergovernmental Tax Credits	NA	NA	\$4,154,255	\$6,180,464	\$6,965,252
Estimated Net Severance Tax Liability	\$26,497,456	\$25,677,079	\$20,761,702	\$18,712,346	\$17,161,561
Average Tax Rate (dollars per ton)	\$0.97	\$0.95	\$0.78	\$0.67	\$0.67

Source: NM Taxation and Revenue Department.

Projections of Severance Tax Revenue from Coal

Coal Severance Tax projections were prepared by the Department of Finance and Administration, based on an analysis of the demand for State coal for in-State electric power generation and for out-of-state uses (primarily power production as well). Usually 13 to 15 million tons per year of New Mexico coal production are burned at the Four Corners and at the San Juan generating stations. The sources for these operations are three mines in San Juan County; Navajo Mine feeds the Four Corners Station, while La Plata and San Juan mines provide coal for San Juan Station. Most of the production from these mines is subject to the severance tax and the severance surtax. Severance tax collections are offset by the Intergovernmental Tax Credit for production on Indian lands that offset severance tax collections on coal by an estimated \$6.9 million in Fiscal Year 2004.

The McKinley Mine in the county of the same name, owned by the Pittsburg & Midway Mining Co. (Chevron Texaco) supplies coal to Arizona power stations. Output from the McKinley Mine was 5.4 million tons in Fiscal Year 2004, a decline from 5.5 million tons in Fiscal Year 2003 and 6.1 million tons in Fiscal Year 2002, with the declining output due to competition from other electricity sources. Most of the declines have been in surtax non-exempt sales, and as a result almost 70 percent of their sales are now surtax exempt.

The Lee Ranch Mine, also in McKinley County, ships coal in varying quantities to Arizona power stations. In addition, the mine provides around 800,000 tons of coal per year to the Escalante Power Station, owned by Plains Electric, which primarily supplies power to rural cooperatives. Total

production at Lee Ranch has increased to 6.8 million tons in Fiscal Year 2004, up from 6.7 million tons in Fiscal Year 2003 and 6.1 million tons in Fiscal Year 2002. These increases have been balanced between surtax-exempt and non-exempt sales.

BHP Billiton Company (including the San Juan Coal Company subsidiary) produced 8.2 million tons in Fiscal Year 2004, down from 15.3 in Fiscal Year 2003 and 14.3 in Fiscal Year 2002. About 33.3 percent of the total are surtax-exempt. In addition, about 20.0 percent of the total—3.0 million tons—is now being produced using underground “long-wall” mining techniques. The San Juan Coal Company implemented the technology in 2001 in order to increase productivity and prolong the life of the mine.

OTHER MINERAL PRODUCTION AND SEVERANCE TAXES

Carbon Dioxide

The Bravo Dome carbon dioxide (“CO₂”) field, encompassing 1.2 million acres in Harding, Union and Quay Counties in the northeastern area of the State, contains estimated resources of 16.3 trillion cubic feet, of which 7.0 to 10.6 trillion cubic feet are considered recoverable. Although the State has long produced limited quantities of liquid and solid CO₂ for use in the food and the engineering industries, the main commercial value of carbon dioxide deposits is derived from 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 CO₂ 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. The wellhead value of CO₂ sales currently is approximately \$0.35 per mcf reported at the production facility, and is expected to remain stable over the forecast period. Severance taxes on CO₂ are levied at the rate of 3.75 percent of sales value.

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 in the following table. 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 revenues.

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Severance Tax Rates and Taxable Values on Other Minerals

<u>Mineral Resources</u>	<u>Tax Rates</u>	<u>Taxable Value as Percent of Full Value</u>
Potash	2.500%	16.67%
Copper	0.500%	16.67% ⁽¹⁾
Timber, Pumice, Gypsum, Sand, Gravel, Clay, Fluorspar, other	0.125%	100.00% ⁽²⁾
Molybdenum	0.125%	50.00%
Lead, Zinc	0.125%	16.67% ⁽¹⁾
Gold	0.200%	50.00% ⁽¹⁾
Silver	0.200%	30.00% ⁽¹⁾
Uranium	3.500%	50.00%

⁽¹⁾ Value based upon the indicated percentage of specified Comex, LME or London spot prices published in Metals Week.

⁽²⁾ 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, which must be processed before sale, deductions are allowed for cost of processing and freight charges to the point of sale.

Source: NM Energy Minerals and Natural Resources Department.

Tax revenue from potash was about \$521,000 in Fiscal Year 2004. Severance tax revenue from copper is limited because of the statutorily defined narrow tax base. Revenue from copper peaked at \$593,000 in Fiscal Year 1996, a result of the combination of high prices and strong production, but most recent revenues were \$154,000 in Fiscal Year 2004. Copper prices have been depressed for the last several years by weakness in world copper prices, but have recently rebounded.

TAXATION OF ENERGY MINERALS NOT PLEDGED

Rates for various property and production taxes on New Mexico minerals are summarized below. As discussed in prior sections of this Official Statement, proceeds from the Severance Tax and the Oil and Gas Severance Tax are pledged via the Bonding Fund to payment of interest, premium and principal of the Bonds. **Proceeds of other taxes shown below are not pledged to the payment of interest, premium or principal of the Bonds.**

Production and Property Taxes on Oil and Gas

Current effective production and property tax rates expressed on *ad valorem* and unit bases are set forth below. The rates and amounts were based on data from Fiscal Year 2004 and reflect an average sales price of \$31.97 per barrel for oil and \$4.68 per thousand cubic feet (mcf) for natural gas. The effective rates presented in the table below show taxes paid as a percentage of gross sales value before subtracting allowable deductions.

**Effective Production and Property Tax Rates on Oil and Gas
Fiscal Year 2004**

	Natural Gas			Crude Oil		
	<u>Effective Tax Rate</u>			<u>Effective Tax Rate</u>		
	<u>Statutory Rate</u>	<u>Percent of Value</u>	<u>Dollars Per mcf</u>	<u>Statutory Rate</u>	<u>Ad valorem</u>	<u>Per Barrel</u>
Oil and Gas School Tax	4.00%	3.20%	\$0.15	3.15%	2.87%	\$ 0.92
Oil and Gas Severance Tax	3.75%	3.00%	\$0.14	3.75%	3.41%	\$ 1.09
Oil and Gas Conservation Tax	0.19%	0.15%	\$0.01	0.19%	0.17%	\$0.06
Natural Gas Processors Tax	0.011%	0.21%	\$0.01	NA	NA	NA
Oil and Gas Production <i>ad valorem</i> Tax	2.10%	0.84%	\$0.04	2.10%	0.96%	\$0.31
Oil and Gas Production Equip. <i>ad valorem</i> Tax	<u>2.10%</u>	<u>0.19%</u>	<u>\$0.01</u>	<u>2.10%</u>	<u>0.17%</u>	<u>\$0.05</u>
Total		7.59%	\$0.36		7.58%	\$2.42
Subtotal—State tax only, excludes <i>ad valorem</i> taxes		6.56%	\$0.31		6.45%	\$2.06

Source: NM Department of Finance and Administration

The School Tax rate of 3.15 percent imposed on natural gas was raised to 4.00 percent effective July 1, 1993, pursuant to Laws 1993, Chapter 360. This action was taken partially to compensate for the large decreases in revenues due to the 1987 tax changes for natural gas. Further, it was believed that the tax increase was tolerable to industry because of relatively higher prices. The School Tax rate imposed on crude oil continues to be 3.15 percent.

Statutory rates on Oil for the School Tax (3.15 percent), the Oil and Gas Severance Tax (3.75 percent) and the Conservation Tax (0.19 percent) are effectively reduced by deductions allowed for trucking costs and for Federal, State and Indian royalties. Statutory rates on natural gas for the School Tax (4.00 percent), the Oil and Gas Severance Tax (3.7 percent), and the Conservation Tax (0.19 percent) are effectively reduced by deductions for Federal, State and Indian royalties and by deductions for transportation and processing tariffs upstream of the sales location. 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 current 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 equipment *ad valorem* tax. The Taxation and Revenue Department is not aware of any wells currently producing commercial helium in the State. However, according to a study by the New Mexico Bureau of Geology and Mineral Resources,⁽²⁾ the State has produced commercial volumes of helium in the recent past. If the historical production volumes are reached in the future, increased taxes on helium and new hydrocarbon gases could generate as much as \$1.3 million in revenue for the Bonding Fund.

⁽²⁾ "Helium in New Mexico: Geologic Distribution and Exploration Possibilities," Ronald F. Broadhead and Lewis Gillard, N.M. Bureau of Geology and Mineral Resources.

Production Taxes on Coal

Total State production taxes on coal amounted to over \$22 million in Fiscal Year 2004. Total coal production was just under 25.6 million tons in that year. Thus, the average effective tax per ton was approximately \$0.86. With total sales revenue of over \$583 million, the average effective tax was 3.77 percent of total sales revenue. The breakout of the effective tax and the total amount collected for each tax is shown in the following table.

Effective Production Taxes on Coal Fiscal Year 2004

	Surface-Mined Coal <u>Subject to Severance Surtax</u>			Surface-Mined Coal <u>Subject to Severance Surtax</u>		
	<u>Effective Tax Rate</u>			<u>Effective Tax Rate</u>		
	<u>Statutory Rate</u>	<u>Percent of Value</u>	<u>Dollars Per Ton</u>	<u>Statutory Rate</u>	<u>Percent of Value</u>	<u>Dollars \$ Per Ton</u>
Severance Tax	\$ 0.57	2.60%	\$ 0.59	\$ 0.57	2.85%	\$ 0.65
Severance Surtax	\$ 0.60	3.00%	\$ 0.68	\$ 0.00	0.00%	\$ 0.00
Resources Excise Tax	0.75%	0.75%	\$ 0.17	\$ 0.75%	0.75%	\$ 0.17
Oil and Gas Conservation Tax	0.19%	0.19%	\$ 0.04	\$ 0.19%	0.19%	\$ 0.04
Property Tax	<u>2.50%</u>	<u>0.50%</u>	<u>\$ 0.11</u>	<u>\$ 2.50%</u>	<u>0.50%</u>	<u>\$ 0.11</u>
Total		7.04%	\$ 1.61		4.29%	\$ 0.98
Subtotal—State tax only		6.54%	\$ 1.49		3.79%	\$ 0.86

Statutory rates for the Resources Excise 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.

BOOK-ENTRY-ONLY SYSTEM

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that the State and the Underwriters believe to be reliable, but neither the State or the Underwriters take responsibility for the accuracy thereof.

The Depository Trust Company ("DTC"), New York, New York, will act as securities depository for the Bonds. The Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Bond certificate will be issued for each issue of the Bonds, each in the aggregate principal amount of such issue, and will be deposited with DTC.

DTC, the world's largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2.2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 100 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of

securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Fixed Income Clearing Corporation and Emerging Markets Clearing Corporation, (NSCC, FICC and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org.

Purchases of Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC’s records. The ownership interest of each actual purchaser of each Bond (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations provided details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC’s records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices shall be sent to DTC. If less than all of the Bonds of a maturity are being redeemed, DTC’s practice is to determine by lot the amount of the interest of each Direct Participant to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Bonds unless authorized by a Direct Participant in accordance with DTC’s Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the State as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.’s consenting or voting rights to those Direct Participants to whose accounts Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, distributions and dividend payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC’s practice is to credit Direct Participants’ accounts upon DTC’s receipt of funds and corresponding detail

information from the State, on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC nor its nominee, or the State, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the State, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Bonds at any time by giving reasonable notice to the State. Under such circumstances, in the event that a successor depository is not obtained, Bond certificates are required to be printed and delivered.

The State may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered to DTC.

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that the State and the Underwriters believe to be reliable, but neither the State nor the Underwriters take any responsibility for the accuracy thereof.

THE STATE WILL NOT HAVE ANY RESPONSIBILITY OR OBLIGATION TO THE DTC PARTICIPANTS OR BENEFICIAL OWNERS.

SO LONG AS CEDE & CO., AS NOMINEE OF DTC, IS THE REGISTERED OWNER OF THE BONDS, REFERENCES HEREIN TO THE BONDHOLDERS OF THE BONDS WILL MEAN CEDE & CO., AND WILL NOT MEAN THE BENEFICIAL OWNERS OF THE BONDS.

When reference is made to any action which is required or permitted to be taken by the Beneficial Owners, such reference only relates to those permitted to act by statute, regulation or otherwise on behalf of such Beneficial Owners for such purposes. When notices are given, they are to be sent to DTC, and the State does not have responsibility for distributing such notices to the Beneficial Owners.

The State does not have any responsibility or obligation to the DTC Participants or the Beneficial Owners with respect to (a) the accuracy of any records maintained by DTC or any DTC Participant; (b) the payment by DTC or any DTC Participant of any amount due to any Beneficial Owner in respect of the principal of and premium, if any, and interest on the Bonds; (c) the selection of the Beneficial Owners to receive payment in the event of any partial redemption of the Bonds; (d) any consent given or other action taken by DTC, or its nominee, Cede & Co., as Bond Owner; or (e) the distribution by DTC to DTC Participants or Beneficial Owners of any notices received by DTC as registered owner of the Bonds.

SUMMARY OF CERTAIN PROVISIONS OF THE BOND RESOLUTION

The following summarizes certain provisions of the Bond Resolution. This summary does not purport to be complete and reference is made to the Bond Resolution for a full and complete statement of its provisions.

Covenants

So long as any Bonds are outstanding, the State and the Board have covenanted and agreed with the owners of Bonds that: (a) the State will use its best efforts to collect and deposit in the Bonding Fund proceeds from Severance Taxes as set forth in the Severance Tax Bonding Act which, when combined with other amounts the State Legislature, in its sole discretion, may from time to time deposit in the Bonding Fund, will equal at least two hundred (200) percent of the amount of the principal of and interest scheduled to be due in each Fiscal Year of the State on the Senior Severance Tax Bonds including the Series 2005B-1 Bonds, and will equal at least one hundred sixty (160) percent of the amount of the principal of and interest scheduled to be due in each Fiscal Year of the State on the Senior Severance Tax Bonds and the Supplemental Severance Tax Bonds, including the Series 2005B-2 Bonds; (b) the State will promptly pay the principal of and the interest on the Bonds, at the places, on the dates and in the manner specified in the Bond Resolution and in the Bonds; (c) the State will keep proper books of record and account, separate and apart from all other records and accounts, showing complete and correct entries of all transactions relating to Severance Taxes, the Bonding Fund and each project account; (d) any registered owner or Beneficial Owner of any of the Bonds or any duly authorized agent of such registered owner or Beneficial Owner, shall have the right, at all reasonable times, to inspect all records, accounts and data relating to the Bonds, the collection of Severance Taxes and the Bonding Fund; provided, however, that pursuant to Section 6-14-10E NMSA 1978, records with regard to the ownership of or pledges of the Bonds are not subject to inspection or copying; (e) the State will prepare annual statements or audits of collections and disbursements of Severance Taxes in sufficient detail to show compliance with requirements of the Bond Resolution and the State will furnish a copy of such audit to any owner of Bonds upon written request therefor; (f) in order to prevent any accumulation of claims for interest after maturity, the State will not directly or indirectly extend or assent to the extension of time for the payment of interest on any of the Bonds; (g) the State will make no use of the proceeds of the Bonds or any funds reasonably expected to be used to pay the Bonds which will cause the Bonds to be arbitrage bonds within the meaning of Section 148 of the Internal Revenue Code of 1986, as amended (the "Code") which would result in the loss of the exclusion from gross income for federal income tax purposes of the interest on the Bonds; (h) the State will take or cause to be taken such actions which may be required of it for the interest on the Bonds to be and remain excluded from gross income for federal income tax purposes; and (i) the State will not take or permit to be taken any actions which would adversely affect that exclusion, and the State or persons acting for it, will, if necessary to maintain such exclusion, among other acts of compliance, (1) apply, or cause to be applied, the proceeds of the Bonds to the purpose of the borrowing, (2) restrict the yield on investment-type property acquired with those proceeds, (3) make timely rebate payments to the federal government in accordance with Section 148 of the Code and the Bond Resolution, (4) maintain books and records and make calculations and reports, and (5) refrain from certain uses of proceeds, all in such manner and to the extent necessary to assure such exclusion of that interest under the Code.

Defeasance

If the State shall pay all of the outstanding Bonds, or shall cause them to be paid and discharged in accordance with the next paragraph of this section, or if all payments of principal of and interest on the Bonds, due or to become due, shall otherwise be paid to the owners of the outstanding Bonds, then the Bond Resolution shall cease and become null and void (except for those provisions surviving in accordance with the last paragraph of this section), and the covenants, agreements and obligations of the Board and the State under the Bond Resolution shall be released, discharged and satisfied.

All or any part of the Bonds shall be deemed to have been paid and discharged if: (1) the Registrar/Paying Agent shall, in advance of any payment to the owners of the outstanding Bonds, have received sufficient moneys for the payment in full of the principal of and interest on the Bonds, or part

thereof, or (2) there shall have been placed in trust for the payment of the Bonds and irrevocably committed to such payment, non-callable Defeasance Obligations (defined below) which are certified by an independent public accounting firm of national reputation to be of such maturities or redemption dates and interest payment dates, and scheduled to bear such interest, as will be sufficient, together with any moneys on deposit with the Registrar/Paying Agent available to pay principal of and interest on the Bonds, without further investment or reinvestment of either the principal amount or the interest earnings on such Defeasance Obligations (which earnings are to be held likewise in trust and so committed, except as provided herein), for the payment in full of all principal of and interest on the Bonds, or part of the Bonds, deemed to have been paid, at their maturity.

As used in the Bond Resolution, “Defeasance Obligations” means, as permitted by law:

(i) direct obligations of, or obligations the full and timely payment of the principal of and interest on which is unconditionally guaranteed by, or obligations issued by or backed by the full faith and credit of corporations sponsored by, the United States of America;

(ii) obligations issued or guaranteed as to full and timely payment of principal and interest by any agency or person controlled by and acting as an instrumentality of the United States of America, pursuant to authority granted by the Congress of the United States of America; and

(iii) obligations described in Section 103(a) of the Code (a) provisions for the payment of the principal of, premium, if any, and interest on which (1) shall have been made by the irrevocable deposit, with a bank or trust company acting as a trustee or escrow agent for holders of such obligations, of non-callable securities described in clauses (i) and (ii) above, the maturing principal of and interest on which, when due and payable, without further investment or reinvestment, will provide sufficient moneys to pay when due the principal of and interest on such obligations, and (2) which securities described in clause (i) and (ii) are not available to satisfy year any other claim, including any claim of such trustee or escrow agent or of any person claiming through such trustee or escrow agent or to whom such trustee or escrow agent may be obligated, including claims in the event of the insolvency of such trustee or escrow agent or proceedings arising out of such insolvency or (b) rated by either Standard & Poor’s Rating Group or Moody’s Investors Service, Inc., or similar rating agency in its highest rating category (without regard to any refinement or gradation by numerical modifier or otherwise).

Any moneys held in trust in accordance with the defeasance provisions of the Bond Resolution may be invested only in non-callable Defeasance Obligations having maturity dates, or having redemption dates which, at the option of the holder of such Obligations, shall not be later than the date or dates at which moneys will be required for the purposes described above. Within fifteen (15) days after any Bonds are deemed to be paid and discharged, a written notice of such deemed payment and discharge shall be given to each registered owner of Bonds as shown on the registration books kept by the Registrar/Paying Agent on the date on which such Bonds are deemed paid and discharged. Such notice shall state the numbers of the Bonds deemed paid and discharged or state that all Bonds are deemed paid and discharged and set forth a description of the obligations held.

Notwithstanding that Bonds may be deemed to have been paid, any provisions of the Bond Resolution which relate to the maturity of Bonds, interest payments and dates thereof, exchange, transfer and registration of Bonds, replacement of mutilated, destroyed, lost or stolen Bonds, the safekeeping and cancellation of Bonds, nonpresentment of Bonds, and the duties of the Registrar/Paying Agent in connection with all of the foregoing, shall remain in effect and be binding upon the State and the Registrar/Paying Agent until final payment of all Bonds notwithstanding the release and discharge of the Bond Resolution. Notwithstanding any provision of the Bond Resolution to the contrary, any provisions

of the Bond Resolution which relate to the exclusion of interest from gross income for federal tax purposes shall remain in effect and be binding upon the State and the Registrar/Paying Agent.

Amendment of Bond Resolution

The Bond Resolution may be amended or supplemented from time to time without the consent of or notice to the holders of the Bonds for any of the following purposes: (a) to cure any ambiguity, omission, formal defect or inconsistency, or (b) to make any change that, in the judgment of the Board, in reliance upon an opinion of counsel, does not have a material adverse effect on the rights of the owners of any Bonds, or (c) to achieve compliance with any applicable federal securities or tax laws or to ensure the exclusion of interest on the Bonds from the gross income of the owners of the Bonds for federal income tax purposes.

Except as provided above, the Bond Resolution may only be amended or supplemented by resolution adopted by the Board in accordance with applicable law, with or without receipt by the State of any additional consideration, but with the written consent of the owners of a majority in principal amount of the Bonds then outstanding; provided, however, that no such resolution shall have the effect of permitting: (i) an extension of the maturity of any Bond; or (ii) a reduction in the principal amount of, the rate of interest on, or the redemption premium on any Bond; or (iii) a reduction of the principal amount of Bonds required for consent to such amendatory or supplemental resolution; or (iv) the establishment of priorities as between Bonds issued and outstanding under the provisions of the Bond Resolution; or (v) the modification of, or otherwise affecting, the rights of the owners of less than all of the Bonds then outstanding.

Remedies of Holders of Bonds

The registered owners, or Beneficial Owners, of not less than 25 percent in aggregate principal amount of the Severance Tax Bonds or Supplemental Severance Tax Bonds then outstanding may bring an action to protect the rights of the registered owners and Beneficial Owners of Bonds under the Bond Resolution in any court of competent jurisdiction, for the specific performance of any covenant or agreement contained in the Bond Resolution or to enjoin any act or thing which may be unlawful or in violation of any right of any owner of the Bonds. All such proceedings at law or in equity shall be instituted, had and maintained for the equal benefit of all owners of the Bonds then outstanding. The failure of any registered owner or owners or Beneficial Owner or Beneficial Owners of Bonds to so proceed shall not relieve the State or the Board of any obligation to perform any duty under the Bond Resolution. Each right or privilege of such owner and Beneficial Owner is in addition and cumulative to any other right or privilege, and the exercise of any right or privilege by or on behalf of any registered owner or Beneficial Owner shall not be deemed a waiver of any other right or privilege.

Payment of Principal and Interest

The Bonds and the interest accruing on the Bonds shall be payable and collectible out of the Bonding Fund, which is pledged for such payment as provided in the Severance Tax Bonding Act. Interest on the Bonds shall be payable by check or draft mailed to their registered owners, as shown on the registration books for the Bonds maintained by the Registrar/Paying Agent at the address appearing in such books at the close of business on the fifteenth (15th) day of the calendar month next preceding each applicable interest payment date (the "Record Date") or in such other manner as may be agreed upon by the Registrar/Paying Agent and the registered owner of a Bond. Interest which is not timely paid or duly provided for shall cease to be payable to the owners of the Bonds (or of one or more predecessor Bonds) as of the Record Date, but shall be payable to the registered owners of the Bonds (or of one or more predecessor Bonds) at the close of business on a special record date (the "Special Record Date") for the

payment of that overdue interest to be fixed by the Registrar/Paying Agent. The Special Record Date shall be fixed by the Registrar/Paying Agent whenever moneys become available for payment of the overdue interest, and notice of the Special Record Date shall be given to owners of Bonds not less than ten (10) days prior to such date. The principal of the Bonds is payable upon presentation and surrender of the Bonds without deduction for exchange or collection charges at the office of the Registrar/Paying Agent. Principal of and interest on the Bonds are payable in lawful money of the United States of America.

While registered in the name of DTC or its nominee, payments of principal of and interest on the Bonds shall be made to DTC or its nominee as set forth in the Letter of Representation between DTC and the State.

TRANSCRIPT AND LEGAL OPINIONS

The Board will furnish an official transcript of proceedings of the authorization and issuance of the Bonds.

Legal matters incident to the issuance of the Bonds and the exclusion from gross income for Federal and State of New Mexico income tax purposes of interest on the Bonds (see “TAX MATTERS” below and the form of opinion of Bond Counsel attached hereto as Appendix D) are subject to the approving legal opinion of Sutin Thayer & Browne A Professional Corporation, Bond Counsel to the State. A copy of the approving opinion of Bond Counsel, dated and speaking as of the date of original delivery of the Bonds, will be included on the back of each of the Bonds delivered to DTC. Certain legal matters will be passed upon for the State of New Mexico by Brownstein Hyatt & Farber, P.C., Disclosure Counsel. Certain legal matters will be passed upon for the Underwriters by McCall Parkhurst & Horton L.L.P. and Scheuer, Yost & Patterson, P.C. Certain legal matters will be passed upon for the State of New Mexico by the Office of the Attorney General of the State of New Mexico.

TAX MATTERS

In the opinion of Sutin, Thayer & Browne A Professional Corporation (“Bond Counsel”), based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Bonds is excludable from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 (the “Code”) and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, such interest is taken into account in determining adjusted current earnings for the purpose of computing the alternative minimum tax on certain corporations. Bond Counsel is further of the opinion that interest on the Bonds is exempt from State of New Mexico personal income taxes. A copy of the proposed form of opinion of Bond Counsel is set forth in Appendix D hereto.

To the extent the issue price of any maturity of Bonds is less than the amount to be paid at maturity of such Bonds (excluding amounts stated to be interest and payable at least annually over the term of such Bonds), the difference constitutes “original issue discount,” the accrual of which, to the extent properly allocable to each Beneficial Owner thereof, is treated as interest on the Bonds which is excluded from gross income for federal income tax purposes. For this purpose, the issue price of a particular maturity of the Bonds is the first price at which a substantial amount of such maturity of the Bonds is sold to the public (excluding bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers). The original issue discount with respect to any maturity of the Bonds accrues daily over the term to maturity of such Bonds on the basis of a constant interest rate compounded semiannually (with straight-line interpolations between compounding

dates). The accruing original issue discount is added to the adjusted basis of such Bonds to determine taxable gain or loss upon disposition (including sale, redemption, or payment on maturity) of such Bonds. Beneficial Owners of the Bonds should consult their own tax advisors with respect to the tax consequences of ownership of Bonds with original issue discount, including the treatment of Beneficial Owners who do not purchase such Bonds in the original offering to the public at the first price at which a substantial amount of such Bonds is sold to the public.

Bonds purchased, whether at original issuance or otherwise, for an amount higher than their principal amount payable at maturity (or, in some cases, at their earlier call date) ("Premium Bonds") will be treated as having amortizable bond premium. No deduction is allowable for the amortizable bond premium in the case of bonds, like the Premium Bonds, the interest on which is excluded from gross income for federal income tax purposes. However, the amount of tax-exempt interest received, and a Beneficial Owner's basis in a Premium Bond, will be reduced by the amount of amortizable bond premium properly allocable to such Beneficial Owner. Beneficial Owners of Premium Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Bonds. The Issuer has made certain representations and covenanted to comply with certain restrictions, conditions and requirements designed to ensure that interest on the Bonds will not be included in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in interest on the Bonds being included in gross income for federal income tax purposes, possibly from the date of original issuance of the Bonds. The opinion of Bond Counsel assumes the accuracy of these representations and compliance with these covenants. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken), or events occurring (or not occurring), or any other matters coming to Bond Counsel's attention after the date of issuance of the Bonds may adversely affect the value of, or the tax status of interest on, the Bonds.

Certain requirements and procedures contained or referred to in the Bond Resolution and the Tax Certificate and other relevant documents may be changed and certain actions (including, without limitation, defeasance of Bonds) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. Bond Counsel expresses no opinion as to any Bond or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of bond counsel other than Bond Counsel.

Although Bond Counsel is of the opinion that interest on the Bonds is excludable from gross income for federal income tax purposes, is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations (however, such interest is taken into account in determining adjusted current earnings for the purpose of computing the alternative minimum tax on certain corporations), and is exempt from State of New Mexico personal income taxes, the ownership or disposition of, or the accrual or receipt of interest on, the Bonds may otherwise affect a Beneficial Owner's federal, state or local tax liability. The nature and extent of these other tax consequences depends upon the particular tax status of the Beneficial Owner or the Beneficial Owner's other items of income or deduction. Bond Counsel expresses no opinion regarding any such other tax consequences.

Future legislation, if enacted into law, or clarification of the Code may cause interest on the Bonds to be subject, directly or indirectly, to federal income taxation, or otherwise prevent Beneficial Owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such future legislation or clarification of the Code may also affect the market price for,

or marketability of, the Bonds. Prospective purchasers of the Bonds should consult their own tax advisers regarding any pending or proposed federal tax legislation, as to which Bond Counsel expresses no opinion.

The opinion of Bond Counsel is based on current legal authority, covers certain matters not directly addressed by such authorities, and represents Bond Counsel's judgment as to the proper treatment of the Bonds for federal income tax purposes. It is not binding on the Internal Revenue Service ("IRS") or the courts. Furthermore, Bond Counsel cannot give and has not given any opinion or assurance about the future activities of the Issuer, or about the effect of future changes in the Code, the applicable regulations, the interpretation thereof or the enforcement thereof by the IRS. The Issuer has covenanted, however, to comply with the requirements of the Code.

Unless separately engaged, Bond Counsel is not obligated to defend the Issuer or the Beneficial Owners regarding the tax-exempt status of the Bonds in the event of an audit examination by the IRS. Under current procedures, parties other than the Issuer and their appointed counsel, including the Beneficial Owners, would have little, if any, right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax-exempt bonds is difficult, obtaining an independent review of IRS positions with which the Issuer legitimately disagrees, may not be practicable. Any action of the IRS, including but not limited to selection of the Bonds for audit, or the course or result of such audit, or an audit of bonds presenting similar tax issues may affect the market price for, or the marketability of, the Bonds, and may cause the Issuer or the Beneficial Owners to incur significant expense.

LITIGATION

At the time of the original delivery of the Bonds, the Board will deliver a no-litigation certificate to the effect that no litigation or administrative action or proceeding is pending, or, to the knowledge of the appropriate State Officials, threatened, restraining or enjoining, or seeking to restrain or enjoin, the issuance and delivery of the Bonds, the effectiveness of the legislation authorizing the issuance of the Bonds, the levying or collecting of any taxes for the payment of the debt service on the Bonds (other than those cases described in Appendix C, which proceedings are not, in the opinion of the State Attorney General, reasonably expected to have a material effect on the bondholders), or contesting or questioning the proceedings and authority under which the Bonds have been authorized and are to be issued, sold, executed or delivered, or the validity of the Bonds.

The State is a party to various legal proceedings seeking damages or injunctive relief and generally incidental to its operations which proceedings are unrelated to the Bonds, and to the security therefor. The ultimate disposition of such proceedings is not presently determinable. Such proceedings are not, in the opinion of the State Attorney General, reasonably expected to have a material adverse effect on the Bonds or the security for the payment of the Bonds for the following reason: Severance Taxes are the primary source of payment for the Bonds which are limited obligations of the State. See Appendix C for a summary of litigation and administrative action or proceedings that impact Severance Taxes.

FINANCIAL ADVISORS

The Board has retained Fiscal Strategies Group, Inc., as Financial Advisor in connection with the preparation of this Official Statement and with respect to the issuance of the Bonds. Fiscal Strategies Group, Inc. has contracted with Public Resources Advisory Group (together with Fiscal Strategies Group, Inc., the "Financial Advisors") in connection with the preparation of this Official Statement and with respect to the issuance of the Bonds. The Financial Advisors are not obligated to undertake, and have not

undertaken to make, an independent verification or to assume responsibility for the accuracy, completeness, or fairness of the information contained in this Official Statement nor the information, covenants and representations contained in any of the Bond documentation with respect to the federal income tax status of the Bonds. The Financial Advisors are independent advisory firms and are not engaged in the business of underwriting, trading or distributing municipal securities or other public securities. The Financial Advisory fee for services performed with respect to the Bonds is contingent upon the issuance and delivery of the Bonds but is payable from the Severance Tax Bonding Fund.

BOND INSURANCE

Payment Pursuant to Insurance Policy

The following information relating to the Series 2005B-2 Bonds has been furnished by Ambac Assurance Corporation (“Ambac Assurance” or, as defined elsewhere herein, the “Bond Insurer”) for use in this Official Statement. Reference is made to Appendix F for a specimen Bond Insurance Policy.

Ambac Assurance has made a commitment to issue a financial guaranty insurance policy (the “Bond Insurance Policy”) relating to the Series 2005B-2 Bonds effective as of the date of issuance of the Series 2005B-2 Bonds. Under the terms of the Bond Insurance Policy, Ambac Assurance will pay to The Bank of New York, in New York, New York or any successor thereto (the “Insurance Trustee”) that portion of the principal of and interest on the Series 2005B-2 Bonds which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor (as such terms are defined in the Bond Insurance Policy). Ambac Assurance will make such payments to the Insurance Trustee on the later of the date on which such principal and interest becomes Due for Payment or within one business day following the date on which Ambac Assurance shall have received notice of Nonpayment from the Paying Agent. The insurance will extend for the term of the Series 2005B-2 Bonds and, once issued, cannot be canceled by Ambac Assurance.

The Bond Insurance Policy will insure payment only on stated maturity dates and on mandatory sinking fund installment dates, in the case of principal, and on stated dates for payment, in the case of interest. If the Series 2005B-2 Bonds become subject to mandatory redemption and insufficient funds are available for redemption of all outstanding Series 2005B-2 Bonds, Ambac Assurance will remain obligated to pay principal of and interest on outstanding Series 2005B-2 Bonds on the originally scheduled interest and principal payment dates, including mandatory sinking fund redemption dates. In the event of any acceleration of the principal of the Series 2005B-2 Bonds, the insured payments will be made at such times and in such amounts as would have been made had there not been an acceleration.

In the event the Paying Agent has notice that any payment of principal of or interest on a Series 2005B-2 Bond which has become Due for Payment and which is made to an Owner by or on behalf of the Board has been deemed a preferential transfer and theretofore recovered from its Owner pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such Owner will be entitled to payment from Ambac Assurance to the extent of such recovery if sufficient funds are not otherwise available.

The Bond Insurance Policy does **not** insure any risk other than Nonpayment, as defined in the Bond Insurance Policy. Specifically, the Bond Insurance Policy does **not** cover:

1. payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity.
2. payment of any redemption, prepayment or acceleration premium.

3. nonpayment of principal or interest caused by the insolvency or negligence of any Trustee, Paying Agent or Bond Registrar, if any.

If it becomes necessary to call upon the Bond Insurance Policy, payment of principal requires surrender of Series 2005B-2 Bonds to the Insurance Trustee together with an appropriate instrument of assignment so as to permit ownership of such Series 2005B-2 Bonds to be registered in the name of Ambac Assurance to the extent of the payment under the Bond Insurance Policy. Payment of interest pursuant to the Bond Insurance Policy requires proof of the Owner's entitlement to interest payments and an appropriate assignment of the Owner's right to payment to Ambac Assurance.

Upon payment of the insurance benefits, Ambac Assurance will become the owner of the Series 2005 B-2 Bond, appurtenant coupon, if any, or right to payment of principal or interest on such Insured Bond and will be fully subrogated to the surrendering Owner's rights to payment.

Ambac Assurance Corporation

The Bond Insurer is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin and licensed to do business in 50 states, the District of Columbia, the Territory of Guam, the Commonwealth of Puerto Rico and the U.S. Virgin Islands, with admitted assets of approximately \$8,585,000,000 (unaudited) and statutory capital of \$5,251,000,000 (unaudited) as of March 31, 2005. Statutory capital consists of the Bond Insurer's policyholders' surplus and statutory contingency reserve. Standard & Poor's Credit Markets Services, a Division of The McGraw-Hill Companies, Moody's Investors Service and Fitch Ratings have each assigned a triple-A financial strength rating to the Bond Insurer.

The Bond Insurer has obtained a ruling from the Internal Revenue Service to the effect that the insuring of an obligation by the Bond Insurer will not affect the treatment for federal income tax purposes of interest on such obligation and that insurance proceeds representing maturing interest paid by the Bond Insurer under policy provisions substantially identical to those contained in its Bond Insurance Policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the obligor of the insured obligation.

The Bond Insurer makes no representation regarding the Series 2005B-2 Bonds or the advisability of investing in the Series 2005B-2 Bonds and makes no representation regarding, nor has it participated in the preparation of, the Official Statement other than the information supplied by the Bond Insurer and presented under the heading, "**BOND INSURANCE.**"

RATINGS

Moody's Investors Service ("Moody's") and Standard & Poor's Ratings Service, a division of The McGraw-Hill Companies, Inc. ("S&P") have assigned underlying (i.e., without regard to a municipal bond insurance policy) long-term ratings of "AA2" and "AA", respectively, to the Bonds. An explanation of the significance of such ratings may be obtained from Moody's at 99 Church Street, New York, New York 10007 and S&P at 55 Water Street, New York, New York 10041, and Fitch at One State Street Plaza, New York, New York 10004.

Moody's and S&P have assigned ratings of "Aaa" and "AAA", respectively, to the Series 2005B-2 Bonds, with the understanding that upon the delivery of the Bonds, a policy insuring the payment when due of the principal of an interest on the Bonds will be issued by a municipal bond insurer. In addition, Moody's and S&P have assigned underlying (i.e., without regard to a municipal bond insurance policy) long-term ratings of "AA3" and "A+", respectively, to the Bonds.

Such ratings reflect only the views of such organizations. The ratings are not a recommendation to buy, sell or hold the Bonds and there is no assurance that such ratings will continue for any given period of time or that such ratings will not be revised downward or withdrawn entirely by the rating agencies if, in their judgment, circumstances so warrant. Any downward revision or withdrawal of the ratings given to the Bonds may have an adverse effect on the market price of the Bonds. The Underwriters have not undertaken any responsibility to bring to the attention of the owners of the Bonds any proposed revision or withdrawals of the ratings on the Bonds, or to oppose any such proposed revision or withdrawal.

CONTINUING DISCLOSURE UNDERTAKING

The Board will agree, by means of a Continuing Disclosure Undertaking (the substantial form of which appears in Appendix E) to be delivered to the purchaser of the Bonds at closing, for the benefit of owners of the Bonds to provide certain Annual Financial Information relating to the State by no later than 210 days after the end of each Fiscal Year of the State, commencing with the Fiscal Year ending June 30, 2005, and to provide notices of occurrence of certain enumerated events, if material. The Board will further agree in the Continuing Disclosure Undertaking that if its audited financial statements are not provided as part of the Annual Financial Information, the Board will provide such audited statements when available. The Annual Financial Information and audited financial statements (when available) will be filed by the Board with each Nationally Recognized Municipal Securities Information Repository and with any New Mexico State Information Depository. The notices of material events will be filed by the Board with the Municipal Securities Rulemaking Board and with any New Mexico State Information Depository. In the event of a failure of the Board to comply with any provision of the Continuing Disclosure Undertaking, any owner of Bonds (including beneficial owners of the Bonds) may seek specific performance by court order from a State court in Santa Fe County, New Mexico.

The Continuing Disclosure Undertaking is being executed by the Board to assist in complying with Rule 15c2-12(b)(5) promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934 (the "Rule"). The Board has never failed to comply in all material respects with any previous undertakings entered in compliance with the Rule. The Continuing Disclosure Undertaking will be in effect from and after the issuance and delivery of the Bonds and shall extend to the earliest of: (i) the date the principal and interest on the Bonds is paid or deemed paid; (ii) the date the Board is no longer an "obligated person" with respect to the Bonds within the meaning of the Rule; and (iii) the date on which those portions of the Rule which require the Continuing Disclosure Undertaking are held invalid or repealed.

UNDERWRITING

RBC Dain Rauscher, Bank of America Securities LLC, Goldman, Sachs & Co., Piper Jaffray & Co., Popular Securities, Inc. and Siebert Brandford Shank & Co. have agreed to purchase the Bonds from the State pursuant to a Bond Purchase Agreement dated May 24, 2005 (the "Bond Purchase Agreement"), at a price of \$62,235,108.11, which reflects the par amount of the Bonds (\$58,135,000.00) (i) plus a reoffering premium of \$4,324,859.65, and (ii) less an underwriter's discount of \$224,751.54. The Underwriters will be obligated to take and pay for all of the Bonds if any are taken. The Underwriters intend to offer the Bonds to the public at the offering prices set forth on the inside cover of this Official Statement. After the initial public offering, the public offering price may be varied from time to time by the Underwriters.

No guaranty can be made that a secondary market for the Bonds will develop or be maintained by the Underwriters or others. Thus, prospective investors should be prepared to hold their Bonds to

maturity. In addition, the Underwriters may allow commissions or discounts from such initial offering prices to dealers and others.

APPROVAL BY FINANCE COUNCIL

On May 23, 2003, Governor Bill Richardson signed Executive Order No. 2003-017 establishing the Governor's Finance Council to oversee and approve bond transactions issued by State agencies. The Board has requested approval of the issuance of the Bonds from the Governor's Finance Council and expects to receive the approval prior to the delivery of the Bonds.

VERIFICATION OF MATHEMATICAL CALCULATIONS

Prior to the delivery of the Bonds, Causey Demgen & Moore Inc., Denver, Colorado, Certified Public Accountants & Consultants, will deliver a report on the mathematical accuracy of certain computations contained in schedules provided to them by the Underwriters relating to the adequacy of the maturing principal amounts of the securities held by the Escrow Agent and interest to be earned thereon to pay all the principal of, premium, if any, and interest on the Refunded Bonds when due.

Based on the mathematical computations of the accountants, the Series 2005B-1 Bonds Escrow Accounts will be funded in an amount sufficient such that the Senior Refunded Bonds to be refunded with proceeds of the Series 2005B-1 Bonds will be deemed to have been paid and will no longer be outstanding as of the date of the establishment of the Series 2005B-1 Escrow Account.

Based on the mathematical computations of the accountants, the Series 2005B-2 Bonds Escrow Accounts will be funded in an amount sufficient such that the Supplemental Refunded Bonds to be refunded with proceeds of the Series 2005B-2 Bonds will be deemed to have been paid and will no longer be outstanding as of the date of the establishment of the Series 2005B-2 Escrow Account. See "PLAN OF FINANCING" herein.

MISCELLANEOUS

The foregoing summaries, descriptions and references do not purport to be comprehensive or definitive, and such summaries, descriptions and references are qualified in their entirety by reference to each statute, document, exhibit or other materials summarized or described. The instruments and other materials referred to in this Official Statement may be examined, or copies thereof will be furnished in reasonable amounts, upon written request to the NM State Board of Finance, 131 South Capitol Street, Bataan Memorial Building, Room 181, Santa Fe, New Mexico 87501, or by telephone at (505) 827-4980.

Statements made in this Official Statement involving matters of opinion, forecasts or estimates, whether or not expressly so stated, are intended as such and not as representations of fact. The Appendices are integral parts of this Official Statement and must be read with all other parts of this Official Statement.

This Official Statement has been authorized and issued by the Board.

STATE BOARD OF FINANCE
OF THE STATE OF NEW MEXICO

By /s/ Bill Richardson
President

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APPENDIX A

GENERAL INFORMATION CONCERNING THE STATE OF NEW MEXICO

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GENERAL INFORMATION CONCERNING THE STATE OF NEW MEXICO

The State, admitted as the forty-seventh state on January 6, 1912, is the fifth largest state, containing approximately 121,593 square miles. The State's climate is characterized by sunshine and warm, 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 2 inches (lower Rio Grande Valley) to 300 inches (north central mountains). The State is an experience in comfortable living with its clean air, blue skies and fair weather.

Governmental Organization

The State's government consists of the three branches characteristic of the American political system: executive, legislative and judicial. The executive branch is headed by the Governor elected for a four-year term. A governor may succeed himself in office once. Following a reorganization plan implemented in 1978 to reduce and consolidate some 390 agencies, boards and commissions, the primary functions of the executive branch are now carried out by sixteen cabinet departments, each headed by a cabinet secretary appointed by the Governor.

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. The Board has seven members consisting of the Governor, the Lieutenant Governor, the Treasurer and four members appointed by the Governor with the advice and consent of the Senate; no more than two such appointed members may be from the same political party.

The Department of Finance and Administration, created in 1957 as a part of governmental reorganization measures of that year, 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. On July 1, 1983, the Department of Finance and Administration was reorganized into the DFA, which retained the prior name and handles the State's financial functions, and the General Services Department, which now handles most administrative functions. The executive and administrative head of the DFA is the Secretary, who is appointed by the Governor with the advice and consent of the Senate, and who also serves as Executive Officer of the Board. In 1983, a Board of Finance Division was created in the DFA, to staff and coordinate the functions of the Board.

The Legislature consists of 112 members and is divided into a Senate and a House of Representatives. Senators are elected for four-year terms, members of the House 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. In addition, special sessions of the Legislature may be convened by the Governor, and under certain limited circumstances, extraordinary sessions may be convened by the Legislature. Legislators receive no salary, but do receive per diem and mileage allowances while in session or on official State business.

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

Pension Funds

Two retirement plans, covering most of the employees of the State and its political subdivisions, have been established by statute. These retirement plans are described below. All financing of the plans, including employer and employee contributions and fund investment provisions, as well as all benefit provisions, are established by the Legislature and are not subject to negotiation.

Educational Retirement Association. Total Educational Retirement Board membership as of June 30, 2004 was officially reported as 111,475. The annual actuarial valuation of the Educational Retirement Act of the State was conducted and reported as of June 30, 2004 by Gabriel, Roeder, Smith & Co. The Educational Retirement Board accepted the actuary's conclusion that the existing statutory contributions equal to 7.6 percent by members and 8.65 percent by employers were inadequate to provide for the benefits payable under the system. Accrued assets at fair value on June 30, 2004 were \$6.9 billion and the unfunded liability was \$2.439 billion. As of June 30, 2004, the Educational Retirement Board has an infinite funding period. This is an increase from last year's funding period of 78.0 years. Therefore, if the 8.65 percent employer contribution rate and 7.60 percent member contribution rate remain in place, and all actuarial assumptions are exactly realized, including an 8.00 percent investment return on the actuarial value of assets, then the unfunded liability will never achieve complete amortization. The contribution that would be required in order to amortize the unfunded liability over 40 years is 10.67 percent. Last year the 40-year funding rate was 9.33 percent. Forty years is the maximum funding period under GASB 25, effective through Fiscal Year 2006, when a GASB 25 transition period ends and the maximum amortization period becomes 30 years.

The funded ratio (the ratio of the actuarial value of assets to the actuarial accrued liability) decreased from last year. The funded ratio at June 30, 2003 was 81.1 percent, while the funded ratio at June 30, 2004 is 75.4 percent. Chapter 273, Laws 2005 increases over time employer and employee contributions to the system in order to decrease the unfunded liability and to achieve compliance with GASB 25 regarding the amortization period. Over the course of seven years, overall contributions to the system will increase from 16.25 percent of salaries to 21.8 percent of salaries and the funding period will be reduced to less than 10 years by the early 2020s.

The Public Employees Retirement Association. Gabriel, Roeder, Smith & Co. completed an actuarial valuation of the Public Employees Retirement Fund (PERA), Judicial Retirement Fund, Magistrate Fund, Legislative Division and Volunteer Firefighter Fund (VFF) as of June 30, 2004. 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 5 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. Actuarial information, for each fund, as of June 30, 2004, is shown below.

Summary of State Retirement Funds (dollars in thousands)

	<u>PERA</u>	<u>Judicial</u>	<u>Magistrate</u>	<u>VFF</u>	<u>Legislative</u>
Membership	69,116	207	106	5,546	331
<u>Actuarial Information</u>					
Accrued Liability	\$ 9,950,224.3	\$ 87,620.2	\$30,194.6	\$17,778.2	\$23,530.7
Value of Assets	<u>9,267,268.1</u>	<u>66,208.8</u>	<u>30,071.6</u>	<u>33,000.3</u>	<u>8,407.7</u>
Unfunded (Overfunded) Accrued Liability	\$ 682,956.2	\$ 21,411.4	\$ 123.0	(\$15,222.1)	\$15,123.0
Present Value of Statutory Obligations	\$13,287,899.7	\$113,626.4	\$38,838.2	\$33,721.0	\$25,203.6

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 Severance Tax Bonding Fund and serve as an endowment for future capital projects. In the General Election of 1976, the electorate approved a constitutional amendment giving the Severance Tax Permanent Fund constitutional status. In the General Election of 1982, the electorate approved a second constitutional amendment which removed the discretionary power of the Legislature to appropriate funds from the corpus of the Severance Tax Permanent Fund. Distributions from investments of the 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 invests the corpus and income of the Severance Tax Permanent Fund. The market value of the Severance Tax Permanent Fund as of July 31, 2004 was approximately \$3.62 billion, an increase of approximately 9.0 percent from the prior year. **Money on deposit in the Severance Tax Permanent Fund is not pledged to and may not be used to pay the Bonds.**

The New Mexico State Land Grant Permanent Fund (“LGPF”) is designed solely to benefit the 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), bringing the current total to 8.9 million surface acres and 12.7 million subsurface acres.

The State Land Office is charged with the custody and disposition of the land granted to the State. Through the Commissioner of Public Lands these properties granted to the State are sold and/or leased in accordance with the provisions of the appropriate statutes. The State Investment Officer under the direction of the State Investment Council invests the corpus and income of the LGPF. As of July 31, 2004, the market value of the LGPF was approximately \$7.64 billion, an increase of approximately 12.2 percent from the prior year. **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 the Bonds.** The LGPF is also protected by the Federal Enabling Act of 1910.

In November 1996, the electorate of New Mexico approved a constitutional amendment regarding distributions from the State’s permanent funds. Distributions are now based on a total return basis rather than an income distribution method. Distributions to beneficiaries are 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 electorate of the State of New Mexico approved a constitutional amendment regarding distributions for educational purposes from the State LGPF. The Amendment increases the rate of distribution from the LGPF from 4.7 percent to 5.0 percent of the average Fiscal Year 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 will be distributed in Fiscal Year 2005 through 2012 and an additional 0.5 percent will be distributed in Fiscal Year 2013 through 2016. A three-fifths majority of members elected to each house of the legislature may suspend this additional distribution.

Financial Overview

State Auditing and Accounting Systems. By statute, the financial affairs of every agency in the State are thoroughly examined and audited each year by the State Auditor, personnel of the Auditor's office designated by the Auditor, or by the independent auditors approved by the Auditor. The audits are conducted in accordance with generally accepted auditing standards. The audit reports include financial statements which are presented in accordance with generally accepted accounting principles.

State Budgetary and Appropriation Process. All State agencies are required to submit their budget requests to the Budget Division of the DFA by September 1 of each year following guidelines and forms provided in advance for this purpose. Budget hearings are scheduled for the purpose of examining the merits of budget requests through the fall and are usually completed by mid-December. Statutes require the Budget Division to present comprehensive budget recommendations to the Governor annually by January 2.

By statute, the Governor is required to submit a budget for the upcoming Fiscal Year to the Legislature by the twenty-fifth legislative day. The Governor's budget includes the executive recommendations for higher education, public education and State agencies as well as historical information on prior expenditures and revenues and revenue projections, among other information. The State budget is contained in a General Appropriation Act, which may also contain proposals for supplemental and deficiency appropriations for the then 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 Budget Division of the DFA approves the agency budgets and monitors the expenditure of the funds beginning on July 1, the first day of the Fiscal Year.

Investment Management

By statute the State Treasurer is responsible for the investment of the operating and capital funds of the State. These responsibilities are conducted in accordance with the State Treasurer's Investment Policy adopted by the State Treasurer and approved by the State Board of Finance. The State Treasurer's 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 is subject to review and approval no less than every two years.

The investment policy governs the investment activities of the State Treasurer. This policy applies to all financial assets of the State invested by the Treasurer in the exercise of his statutory authority or invested as directed by other agencies which have specific investment authority and for which the Treasurer acts as agent. These funds include, but are not limited to the State's General Fund, and agency funds such as the Local Government Investment Pool, bond funds, debt service reserve funds, those pension and permanent fund monies not yet allocated to money managers, and all float.

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 Chairman, two members of the State Treasurer's Office involved in the investment decision making process, one of whom will serve as vice-chairman, the Director of the State Board of Finance or designee, and a professional participant in the private investment community or an individual with expert knowledge or professional experience in the subject or professional practice of public

finance or public fund investing, appointed by the State Treasurer with the advice and consent of the State Board of Finance.

The functions of the Investment Committee include:

- Reviewing and recommending, if advisable, modifications in the investment policy of the State Treasurer from time to time;
- Assessing the utility and efficacy of established internal controls as loss prevention measures with respect to the investment portfolio subject to the investing authority of the State Treasurer;
- Determining whether legislation affecting the investment activities of State Treasurer should be recommended;
- Recommending investment procedures that may be useful or required in maintaining currency with public finance market practices;
- Meeting monthly to deliberate such topics as: economic outlook, portfolio diversification and maturity structure, potential risks, the target rate of return on the investment portfolio and the like;
- Identifying potential violations of and suggesting remedial actions to achieve conformity with the investment policy;
- Recommending depositories, custodians, broker/dealers and investment managers and advisors; and
- Assessing whether the investment policy of State Treasurer is being properly implemented by the individuals and entities involved in the administration and management of investment activities.

Economic and Demographic Characteristics

New Mexico is the 36th largest state by population and the fifth largest in land area. The population of the State as of the time of the official 2000 United States Census was 1,819,046. In the 1990's, the State was the 12th fastest growing state, as the population increased 20.1 percent from the 1990 population of 1,515,069. Over the same period of time, the national population grew 13.2 percent.

Most of this population growth is occurring in or near the larger cities. There are three Metropolitan Statistical Areas (MSAs) in the State. The Albuquerque MSA is comprised of Bernalillo, Sandoval and Valencia Counties; the Las Cruces MSA is comprised of Doña Ana County; and the Santa Fe MSA is comprised of Los Alamos and Santa Fe Counties. The fastest growing counties in the state are Torrance, Valencia, Sandoval, Lincoln, Luna and Doña Ana. The following table sets forth information on population growth in New Mexico and nationally over the past decade.

**Population
New Mexico and the United States
1995-2004**

<u>Year</u>	<u>Population</u>		<u>Annual Percentage Change</u>	
	<u>New Mexico</u>	<u>United States</u>	<u>N.M.</u>	<u>U.S.</u>
1995	1,720,394	266,278,393	2.3%	1.2%
1996	1,752,326	269,394,284	1.9%	1.2%
1997	1,774,839	272,646,925	1.3%	1.2%
1998	1,793,484	275,854,104	1.1%	1.2%
1999	1,808,082	279,040,168	0.8%	1.2%
2000	1,821,496	282,192,162	0.7%	1.1%
2001	1,832,335	285,102,075	0.6%	1.0%
2002	1,855,143	287,941,220	1.2%	1.0%
2003	1,878,562	290,788,976	1.3%	1.0%
2004	1,903,289	293,655,404	1.3%	1.0%

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

Major industries in the State are energy resources, semi-conductor manufacturing, tourism, services, arts and crafts, agriculture-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. The following table sets forth information on employment by industry over the period 1980-2000.

Total Full-time and Part-time Employment by Industry

				Growth	
	<u>1980</u>	<u>1990</u>	<u>2000</u>	<u>1980-1990</u>	<u>1990-2000</u>
Total employment	598,199	767,139	972,954	28.2%	26.8%
Wage and salary employment	513,306	635,725	789,690	23.8%	24.2%
Proprietors employment	84,893	131,414	183,264	54.5%	39.7%
Farm proprietors employment	13,400	13,600	14,985	1.5%	10.2%
Nonfarm proprietors employment	71,493	117,814	168,279	64.8%	42.8%
By industry					
Farm employment	22,191	19,766	21,760	-10.9%	10.1%
Nonfarm employment	576,008	747,373	951,194	29.8%	27.3%
Private employment	428,156	568,085	748,804	32.7%	31.8%
Agri. services, forestry, fishing and other	4,358	8,414	13,548	93.1%	61.0%
Mining	31,152	20,489	19,323	-34.2%	-5.7%
Metal mining	10,603	2,187	1,677	-79.4%	-23.3%
Coal mining	1,980	1,781	1,644	-10.1%	-7.7%
Oil and gas extraction	15,116	14,068	14,425	-6.9%	2.5%
Nonmetallic minerals, except fuels	3,453	2,453	1,577	-29.0%	-35.7%
Construction	38,873	40,606	59,895	4.5%	47.5%
General building contractors	11,933	11,858	16,710	-0.6%	40.9%
Heavy construction contractors	8,287	6,729	8,720	-18.8%	29.4%
Special trade contractors	18,653	22,019	34,465	18.0%	56.5%
Manufacturing	35,963	47,732	48,788	32.7%	2.2%
Durable goods	21,583	32,500	33,275	50.6%	2.4%
Nondurable goods	14,380	15,232	15,513	5.9%	1.8%
Transportation and public utilities	30,732	34,130	43,350	11.1%	27.0%
Wholesale trade	22,733	27,896	33,751	22.6%	21.1%
Retail trade	98,075	134,482	172,516	37.1%	28.3%
Finance, insurance, and real estate	37,945	46,955	62,905	23.7%	34.0%
Services	128,325	207,381	294,728	61.6%	42.1%
Government and government enterprises	147,852	179,288	202,390	21.3%	63.1%
Federal, civilian	29,963	31,621	30,205	5.5%	-4.5%
Military	21,794	22,552	17,167	3.5%	-23.9%
State and local	96,095	125,115	155,018	30.2%	23.9%
State governmental	42,560	55,722	64,654	30.9%	16.0%
Local government	53,535	69,393	90,364	29.6%	30.2%

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

The following tables set forth selected additional economic and demographic data with respect to the State.

**Employment and Labor Force
New Mexico and the United States
1995-2004**

<u>Year</u>	<u>Civilian Labor Force</u> (000)		<u>Number of Employed</u> (000)		<u>Unemployment Rate</u>		<u>N.M. as % of U.S. Rate</u>
	<u>New Mexico</u>	<u>United States</u>	<u>New Mexico</u>	<u>United States</u>	<u>New Mexico</u>	<u>United States</u>	
1995	799	132,315	745	117,298	6.8%	5.6%	121%
1996	813	133,951	752	119,708	7.5%	5.4%	139%
1997	823	136,301	769	122,776	6.6%	5.0%	133%
1998	836	137,680	784	125,930	6.2%	4.5%	139%
1999	840	139,380	793	128,993	5.6%	4.2%	133%
2000	851	142,586	809	131,785	5.0%	4.0%	127%
2001	862	143,772	819	131,826	4.9%	4.7%	104%
2002	875	144,862	828	130,341	5.5%	5.8%	95%
2003	893	146,509	841	129,999	5.9%	6.0%	99%
2004	912	147,390	860	131,480	5.7%	5.5%	103%

Source: U.S. Department of Labor, Bureau of Labor Statistics.

**Personal Income
New Mexico and the United States
1995-2004**

<u>Year</u>	<u>Personal Income</u>		<u>Annual Percentage Change</u>	
	<u>New Mexico</u>	<u>United States</u>	<u>N.M.</u>	<u>U.S.</u>
1995	\$31,700,000	\$6,144,741,000	-	-
1996	33,345,192	6,512,485,000	5.2%	6.0%
1997	34,960,814	6,907,332,000	4.8%	6.1%
1998	37,045,765	7,415,709,000	6.0%	7.4%
1999	38,045,599	7,796,137,000	2.7%	5.1%
2000	40,318,443	8,422,074,000	8.8%	8.0%
2001	44,138,165	8,716,992,000	9.5%	3.5%
2002	44,945,537	8,869,809,000	1.8%	1.8%
2003	46,995,434	9,151,694,000	4.6%	3.2%
2004	49,849,350	9,672,205,074	6.1%	5.7%

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

**Per Capita Personal Income
New Mexico and the United States
1995-2004**

<u>Year</u>	<u>Per Capita Income</u>		N.M. as a % <u>of U.S.</u>	<u>Annual Percentage Change</u>	
	<u>New Mexico</u>	<u>United States</u>		<u>N.M.</u>	<u>U.S.</u>
1995	\$18,426	\$23,076	80%	4.5%	4.1%
1996	19,029	24,175	79%	3.3%	4.8%
1997	19,698	25,334	78%	3.5%	4.8%
1998	20,656	26,883	77%	4.9%	6.1%
1999	21,042	27,939	75%	1.9%	3.9%
2000	22,135	29,845	74%	5.2%	6.8%
2001	24,088	30,575	79%	8.8%	2.4%
2002	24,228	30,804	79%	0.6%	0.7%
2003	24,995	31,472	79%	3.2%	2.2%
2004	26,191	32,937	80%	4.8%	4.7%

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

**Wages and Salaries by Industry Sector
1990, 2000 and 2001**

	New Mexico (Dollars in thousands)			United States (Dollars in millions)		Percent Change		Distribution of 2000 Wages & Salaries	
	<u>2001</u>	<u>2000</u>	<u>1990</u>	<u>2000</u>	<u>1990</u>	<u>N.M.</u>	<u>U.S.</u>	<u>N.M.</u>	<u>U.S.</u>
Farm Total	176,072	179,521	95,849	16,781	11,767	87.3%	42.6%	0.8%	0.3%
Non-Farm Private									
Agricultural Services, Forestry, Fishing	153,901	143,971	62,663	30,886	15,164	129.8%	103.7%	0.7%	0.6%
Mining	747,666	671,919	507,585	31,219	26,655	32.4	17.1%	3.1%	0.6%
Construction	1,429,725	1,306,228	577,016	256,807	140,468	126.4%	8.28%	6.0%	5.3%
Manufacturing	1,644,833	1,656,465	980,349	830,026	561,384	69.0%	47.9%	7.6%	17.2%
Transportation & Public Utilities	1,388,489	1,351,378	884,830	313,333	179,390	52.7%	74.7%	6.2%	6.5%
Wholesale Trade	961,496	950,471	552,522	332,549	189,402	72.0%	75.6%	4.4%	6.9%
Retail Trade	2,529,284	2,434,023	1,316,067	449,642	264,791	84.9%	69.8%	11.2%	9.3%
Finance, Insurance & Real Estate	1,066,128	1,027,385	543,814	431,911	207,758	88.9%	107.9%	4.7%	8.9%
Services	6,361,632	5,916,169	2,945,866	1,382,404	644,429	100.8%	114.5%	27.2%	28.6%
Total Private	16,283,154	15,458,009	8,370,712	4,058,777	2,229,441	84.7%	82.1%	71.0%	84.0%
Government									
Federal, Civilian	1,366,112	1,280,241	917,118	135,011	99,598	39.6%	35.6%	5.9%	2.8%
Military	495,168	477,480	440,596	50,520	46,332	8.4%	9.0%	2.2%	1.0%
State & Local	4,700,434	4,374,109	2,472,762	572,880	356,505	76.9%	60.7%	20.1%	11.9%
Total Government	6,561,714	6,131,830	3,830,476	758,411	502,435	60.1%	50.9%	28.2%	15.7%
Non-Farm Total:	22,844,868	21,589,839	12,201,188	4,817,188	2,731,876	76.9%	76.3%	99.2%	99.7%
Total	23,020,940	21,769,360	12,297,037	4,833,969	2,743,643	77.0%	76.2%	100.0%	100.0%

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

APPENDIX B

**STATE OF NEW MEXICO
ANNUAL FINANCIAL AND COMPLIANCE AUDIT REPORT**

YEAR ENDED JUNE 30, 2004

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**STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
ANNUAL FINANCIAL REPORT
JUNE 30, 2004**

(With Independent Auditors' Report Thereon)

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INTRODUCTORY SECTION

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STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Official Roster
June 30, 2004

Office of the State Treasurer

Robert E. Vigil, CPA	State Treasurer
Elaine Olah	Deputy State Treasurer
Ann M. Gallegos	Asst. Deputy State Treasurer

State Treasurer's Investment Committee

Robert E. Vigil, CPA	Chairman
Ann M. Gallegos	Vice-chairman
George Everage	Member
Manny Ortiz	Member
Mark Valdes	State Board of Finance Member

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STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
ANNUAL FINANCIAL REPORT
Year ended June 30, 2004

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STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
ANNUAL FINANCIAL REPORT
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FINANCIAL SECTION

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INDEPENDENT AUDITORS' REPORT

Honorable Bill Richardson, Governor
State Board of Finance
Honorable Robert Vigil, CPA, State Treasurer
Honorable Domingo P. Martinez, CGFM, State Auditor
Santa Fe, New Mexico

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the State of New Mexico, Office of the State Treasurer (State Treasurer) as of and for the year ended June 30, 2004, which collectively comprise the State Treasurer's basic financial statements as listed in the table of contents. We have also audited each fiduciary fund type of the State Treasurer as of and for the year ended June 30, 2004, as displayed in the State Treasurer's basic financial statements. We have also audited Schedules 2 through 5 and Schedules 8 through 9 and Schedule 6 – Summary of Long Term Debt Obligations as listed in the table of contents and included in the financial statements as supplementary information as of and for the year ended June 30, 2004. These financial statements are the responsibility of the State Treasurer's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the financial statements of the State Treasurer, are intended to present the financial position, and the changes in financial position and its budgetary comparisons of only that portion of the governmental activities, each major fund, and the aggregate remaining fund information of the State of New Mexico that is attributable to the transactions of the State Treasurer. They do not purport to, and do not, present fairly the financial position of the State of New Mexico as of June 30, 2004 and the changes in financial position and its budgetary comparisons for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information, as well as each fiduciary fund type of the State Treasurer as of June 30, 2004, and the respective changes in financial position, thereof and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion Schedules 2 through 5 and Schedules 8 through 9 and Schedule 6 – Summary of Long Term Debt Obligations referred to above present fairly, in all material respects, the respective financial and fiduciary funds of the Office of the State Treasurer and the long-term debt obligations of the State of New Mexico as of

June 30, 2004, and the respective changes in financial position where applicable thereof and for the year then ended in conformity with accounting principles generally accepted in the United States of America.

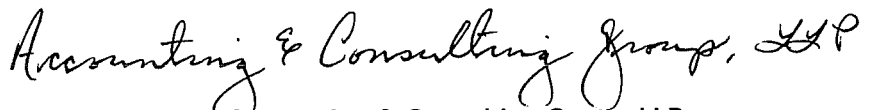
As discussed in Note 19 to the financial statements, the Office of the State Treasurer and the Department of Finance and Administration evaluated financial statement reporting issues related to long-term debt obligations. In previous years, the Office of the State Treasurer reported the State of New Mexico's bond obligations as long-term debt on its government-wide statement of net assets. Since the State of New Mexico, not the Office of the State Treasurer, is obligated for the actual debt, the long-term debt obligations of the State of New Mexico have been removed from the Office of the State Treasurer's government-wide statement of net assets, and will be included in the Department of Finance and Administration's financial statements as an agency fund. A decision was made to include debt service activity in the Office of the State Treasurer's financial statements since the Office of the State Treasurer is responsible, by statute, for making debt service payments on behalf of the State of New Mexico. Accordingly, the debt service activity reported in the Statement of Activities of the Office of the State Treasurer and in the Agency Fund reported in the financial statements of the Department of Finance and Administration will be eliminated during the preparation of the State of New Mexico's Statewide Comprehensive Annual Report (CAFR) and the long-term debt obligations of the State of New Mexico will be reported as part of the Statement of Net Assets in the CAFR. As a result, the June 30, 2003 ending net assets presented in the government-wide statement of net assets of the Office of the State Treasurer have been increased \$761,104,004 to reflect the changes discussed above.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 23, 2004 on our consideration of the State of New Mexico, Office of the State Treasurer's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The *Management's Discussion and Analysis* on pages 5 through 10 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming an opinion on the financial statements that collectively comprise the State Treasurer's basic financial statements. Schedules 1 and 7 as listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. Schedules 1 and 7 as listed in the table of contents have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State Treasurer's basis financial statements. The introductory section is presented for purposes of additional analysis and is not a required part of the basic financial statements. The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.


Accounting & Consulting Group, LLP
Certified Public Accountants

November 23, 2004
Carlsbad, New Mexico

Management's Discussion and Analysis

As management of the OFFICE OF THE STATE TREASURER, we offer readers of the OFFICE OF THE STATE TREASURER'S financial statements this narrative overview and analysis of the financial activities of the OFFICE OF THE STATE TREASURER for the fiscal year ended June 30, 2004. We encourage readers to consider the information presented here in conjunction with the financial statements of the OFFICE OF THE STATE TREASURER and additional information provided.

Financial Highlights

- The assets administered by the OFFICE OF THE STATE TREASURER in the Investment Trust Fund increased by \$416,888,265. The majority of this increase is due to increased average yield on the investment portfolio which has also resulted in increased deposit activity.
- As of the close of the current fiscal year, the OFFICE OF THE STATE TREASURER'S governmental funds reported combined ending fund balances of \$154,065,840, a decrease of \$17,093,210 in comparison with the prior year.
- The Office of the State Treasurer and the Department of Finance and Administration altered the policy related to the reporting of debt. Only debt issued by and for the Office of the State Treasurer should be included in the government-wide financial statements. As a result, the 2004 government-wide financial statements solely include \$83,614 in debt related to compensated absences. This policy change also resulted in a net prior period increase in net assets of \$761,104,004, a \$764,105,000 increase related to debt and a \$3,000,996 decrease related to bond issuance costs net of amortization. Although policy has been changed on the reporting of debt, it should be noted that the Office of the State Treasurer has the statutory responsibility for the overall management and investing of bond proceeds and debt service funds issued by the State Board of Finance. These proceeds require the tracking of all earnings for rebate, arbitrage and interest earnings distribution. The management of these funds begins with the issuance of bonds by the State Board of Finance. On the closing date of bond issuance, funds are delivered to the State Treasurer with identification of sources and uses of the bond proceeds. The State Treasurer then authorizes release of bond funds to the buyer and invests the proceeds in accordance with the State Treasurer's Investment Policy. The State Treasurer administers the distribution of interest earnings on 39 severance-tax bonds, 7 general obligation bonds and 1 miscellaneous bond. All transactions are tracked for the purpose of calculating rebate and arbitrage. In addition, the State Treasurer provides information to the audit firm that prepares the rebate calculations. Management of debt service funds includes monitoring available cash for payment, investing, and cost of issuance. The State Treasurer's Office coordinates with the State Board of Finance cash availability for issuance of one-day notes and determines the amount available for transfer to the state permanent fund as required by statute. Previously issued bonds by the Board of Finance may be re-financed or refunded and acting as the paying agent, the State Treasurer must coordinate payment with escrow agent and Depository Trust Company (DTC).
- A statutory function of the Office of the State Treasurer is to make debt service payments on behalf of State Agencies. As a result, the debt service assets and activity continues to be reported in the governmental funds. Information related to the debt service assets and activity is included in the supplementary information.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the OFFICE OF THE STATE TREASURER'S basic financial statements. The OFFICE OF THE STATE TREASURER'S basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the OFFICE OF THE STATE TREASURER'S finances, in a manner similar to a private-sector business.

The statement of net assets presents information on all of the OFFICE OF THE STATE TREASURER'S assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the OFFICE OF THE STATE TREASURER is improving or deteriorating.

The statement of activities presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

The government-wide financial statements can be found at exhibits A-1 and A-2 of this report.

Fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The OFFICE OF THE STATE TREASURER, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the OFFICE OF THE STATE TREASURER can be divided into two categories: governmental funds, and fiduciary funds.

Governmental Funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The OFFICE OF THE STATE TREASURER maintains five individual governmental funds. Information is presented separately in the governmental fund balance sheet and statement of revenues, expenditures, and changes in fund balances for the general fund, the NM Business Development Corporation fund, the Bond Issuance fund, General Obligation Bond funds, and Severance Tax Bond funds all of which are considered to be major funds. The General Obligation and Severance Tax Bond funds combine into a single, aggregated presentation the activity of each individual bond issue. Individual bond transaction data of these governmental funds is provided in the form of combining statements elsewhere in this report.

The OFFICE OF THE STATE TREASURER adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

The basic governmental fund financial statements can be found at exhibits B-1 through C of this report.

Fiduciary Funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statement because the resources of those funds are not available to support the OFFICE OF THE STATE TREASURER'S own programs.

Fiduciary funds provide the same type of information as the government-wide financial statements, only in more detail. The fiduciary fund financial statements provide separate information for the Short-Term Investment Pool, Consolidated Investment Pool, and State Funds Investment Pool.

The OFFICE OF THE STATE TREASURER'S fiduciary funds account for cash, securities, and other investments identified and held in custody on behalf of local and state government agencies and are separately identified by the types of state and local agencies for which the funds are held. The Short-term Investment Pool accounts for the Local Government Investment Pool (LGIP), the Consolidated Investment Pool accounts for funds held in custody for both state and local government agencies, and the State Funds Investment Pool accounts for funds identified and held in custody on behalf of state agencies.

The basic fiduciary fund financial statements can be found at exhibits D-1 and D-2 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements begin on page 27 of this report.

Other information. The combining statements referred to earlier in connection with the General Obligation and Severance Tax Bond funds are presented immediately following the notes to the financial statements. Combining statements, schedules of capital assets, and schedules of long-term debt can be found on pages 55-79 of this report. Fiduciary schedules are located on pages 80-87.

Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the OFFICE OF THE STATE TREASURER, assets exceeded liabilities by \$154,124,658 at the close of the most recent fiscal year.

By far the largest portion of the OFFICE OF THE STATE TREASURER'S net assets reflect amounts expected to be provided to satisfy its general and severance tax bond obligations. It is the responsibility of the OFFICE OF THE STATE TREASURER to record and administer debt on behalf of the agencies and departments of the State of New Mexico. The proceeds of bond issues authorized by the State Board of Finance are transferred to various State agencies in the form of grants. The Office anticipates the future tax revenues generated will be adequate to service the debt obligations.

An additional portion of the OFFICE OF THE STATE TREASURER'S net assets \$153,988,102 represents resources that are subject to external restrictions on how they may be used.

Governmental activities. Governmental activities decreased the OFFICE OF THE STATE TREASURER'S net assets in the governmental financial statements by \$17,135,725. Key elements of this decrease are as follows:

Comparison of Key Elements

	2004	2003 As Restated
<u>Assets:</u>		
Cash, cash equivalents, and repurchase agreements	\$ 153,873,552	\$ 150,551,828
Due from other agencies	15,300,653	21,407,334
Accrued interest receivable	178,949	947,559
Investment in NM Business Development Corp.	1,363,164	1,665,175
Deferred charges, net	-	-
Capital assets, net	142,432	168,647
Total assets	<u>\$ 170,858,750</u>	<u>\$ 174,740,543</u>
<u>Liabilities and net assets:</u>		
Accounts payable and other	\$ 16,650,478	\$ 3,412,846
Compensated absences, amounts due in one year	74,000	-
Compensated absences, amounts due beyond one year	9,614	67,314
Total liabilities	<u>16,734,092</u>	<u>3,480,160</u>
Net assets:		
Invested in capital assets	142,432	168,647
Restricted	153,988,102	171,274,740
Unrestricted	(5,876)	(183,004)
Total liabilities and net assets	<u>\$ 170,858,750</u>	<u>\$ 174,740,543</u>
	2004	2003
<u>Revenues</u>		
Federal funds	\$ 40,333	\$ 31,905
State appropriation	3,351,800	3,134,200
Interest income	13,682,031	17,450,646
Miscellaneous	-	291,618
Total revenues	<u>17,074,164</u>	<u>20,908,369</u>
<u>Expenses</u>		
Current:		
Personnel services and employee benefits	2,267,100	2,300,001
Operating costs	818,445	814,064
Contractual services	173,942	78,350
Other administrative expenditures	-	10,424
Debt service:		
Interest on long-term debt	264,435,893	132,255,324
Debt service activity	28,223,473	-
Other charges	2,697,020	2,182,543
Nonoperating (revenue) and expense	(264,405,984)	29,649,339
Total expenses	<u>34,209,889</u>	<u>167,290,045</u>
Change in net assets	<u>(17,135,725)</u>	<u>(146,381,676)</u>
Net assets - beginning, as restated	171,260,383	317,642,059
Net assets - ending	<u>\$ 154,124,658</u>	<u>\$ 171,260,383</u>

Financial Analysis of the Government's Funds

As noted earlier, the OFFICE OF THE STATE TREASURER uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds. The focus of the OFFICE OF THE STATE TREASURER'S governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the OFFICE OF THE STATE TREASURER'S financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the OFFICE OF THE STATE TREASURER'S governmental funds reported combined ending fund balances of \$154,065,840, a decrease of \$17,093,210 in comparison with the prior year. Approximately 99.06 percent of this total amount, \$152,624,938 is unreserved, designated for subsequent year's expenditures that is an internal designation of unreserved fund balance. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed to encumbrances and the New Mexico Business Development Corporation, \$1,502,424. The remainder, less than 1%, reported as undesignated, is subject to reversion (if positive) to the State Permanent Fund.

The fund balance of the OFFICE OF THE STATE TREASURER'S general fund increased by \$193,428 during the current fiscal year.

General Fund Budgetary Highlights

Differences between the original budget and the final amended budget are briefly summarized as follows:

- \$253,000 in decreases for personnel services and employee benefits due to several positions remaining open.
- \$337,117 in increases for operating costs for rent, maintenance, repair and replacement of computer software and equipment.

Capital Asset and Debt Administration

Capital assets. The OFFICE OF THE STATE TREASURER'S investment in capital assets for its governmental activities as of June 30, 2004, amounts to \$142,432 (net of accumulated depreciation). This investment in capital assets includes office and computer equipment.

Additional information on the OFFICE OF THE STATE TREASURER'S capital assets can be found in Note 4 of this report.

Long-term debt. At the end of the current fiscal year, the OFFICE OF THE STATE TREASURER was responsible for administering debt service payments on total bonded debt outstanding of \$735,990,000 all of which is secured by pledged tax revenues.

	Total	
	2004	2003
General obligation bonds	\$ 249,150,000	\$ 290,700,000
Severance tax bonds	486,840,000	473,405,000
	<u>\$ 735,990,000</u>	<u>\$ 764,105,000</u>

Additional information on long-term debt administered by the OFFICE OF THE STATE TREASURER can be found in Note 19 and Schedule 6 of this report.

Economic Factors and Next Year's Budgets and Rates

- Inflationary trends in the region compare favorably to national indices. Costs associated with the general fund are expected to remain stable.
- During fiscal year end June 30, 2004, several personnel positions remained open, causing the budget to be underspent. The June 30, 2005 budget anticipates filling those positions.

These factors were considered in preparing the OFFICE OF THE STATE TREASURER'S budget for the 2005 fiscal year.

Request for Information

This financial report is designed to provide a general overview of the OFFICE OF THE STATE TREASURER'S finances for those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Robert Vigil, State Treasurer, OFFICE OF THE STATE TREASURER, P. O. Box 608, Santa Fe, NM 87504-0608.

BASIC FINANCIAL STATEMENTS

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
STATEMENT OF NET ASSETS
June 30, 2004

Exhibit A-1

	<u>Governmental Activities</u>
ASSETS	
Cash and cash equivalents	\$ 324,519
Repurchase agreements	153,549,033
Due from other agencies	15,300,192
Accrued interest receivable	178,949
Other receivables	461
Investment in New Mexico Business Development Corporation	1,363,164
Capital assets (net of accumulated depreciation):	
Equipment	<u>142,432</u>
Total assets	<u><u>\$ 170,858,750</u></u>
LIABILITIES AND NET ASSETS	
Accounts payable and other current liabilities	\$ 247,242
Due to Severance Tax Permanent Fund	16,318,268
Noncurrent liabilities:	
Due within one year	74,000
Due in more than one year	9,614
Accrued arbitrage interest payable	<u>84,968</u>
Total liabilities	<u>16,734,092</u>
Invested in capital assets, net of related debt	142,432
Restricted for:	
Debt service	148,568,408
Debt service-arbitrage	4,056,530
New Mexico Business Development Corporation	1,363,164
Unrestricted	<u>(5,876)</u>
Total net assets	<u>154,124,658</u>
Total liabilities and net assets	<u><u>\$ 170,858,750</u></u>

The accompanying notes are an integral part of these financial statements.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
STATEMENT OF ACTIVITIES
For the year ended June 30, 2004

Exhibit A-2

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenues</u>	<u>Net (Expenses) Revenue and Changes in Net Assets</u>
		<u>Operating Grants and Contributions</u>	<u>Primary Governmental Activities</u>
Primary government:			
Governmental activities:			
Personnel services and employee benefits	\$ 2,267,100	\$ 40,333	\$ (2,226,767)
Operating costs	818,445	-	(818,445)
Contractual services	173,942	-	(173,942)
Other charges	2,697,020	-	(2,697,020)
Interest on long-term debt	264,435,893	-	(264,435,893)
Total governmental activities	<u>270,392,400</u>	<u>40,333</u>	<u>(270,352,067)</u>
General Revenues:			
State general fund appropriations			3,351,800
State property tax levy			52,192,007
Severance taxes			311,007,941
Other taxes			732,270
Capital projects - reversions in			3,512,562
Severance tax permanent fund - reversions out			(16,318,268)
Miscellaneous			(290,528)
Unrestricted investment earnings			13,682,031
Net effect of debt service transactions			(28,223,473)
Bond appropriations expense			<u>(86,430,000)</u>
Total general revenues and transfers			<u>253,216,342</u>
Change in net assets			<u>(17,135,725)</u>
Net assets - beginning, as previously stated			(589,843,621)
Increase resulting from change in reporting of debt administered by the Office of the State Treasurer			764,105,000
Decrease resulting from change in reporting of bond issuance costs related to debt administered by the Office of the State Treasurer			<u>(3,000,996)</u>
Net assets - beginning of year, as restated			<u>171,260,383</u>
Net assets - ending			<u><u>\$ 154,124,658</u></u>

The accompanying notes are an integral part of these financial statements.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
BALANCE SHEET
GOVERNMENTAL FUNDS
June 30, 2004

	General	NM Business Development Corp. Fund
ASSETS		
<i>Cash and Investments:</i>		
Cash and cash equivalents	\$ 324,519	\$ -
Repurchase agreements	-	-
Total Cash and Investments	<u>324,519</u>	<u>-</u>
<i>Restricted Assets:</i>		
Investment in New Mexico Business Development Corporation	-	1,363,164
<i>Other Assets:</i>		
Due from other agencies	-	-
Other receivables	461	-
Accrued interest receivable	-	-
<i>Total Assets</i>	<u>\$ 324,980</u>	<u>\$ 1,363,164</u>
LIABILITIES AND FUND BALANCES		
<i>Liabilities:</i>		
Accounts payable and accrued expenses	226,195	\$ -
Due to State General Fund	21,047	-
Due to Severance Tax Permanent Fund	-	-
Accrued arbitrage interest payable	-	-
<i>Total liabilities</i>	<u>247,242</u>	<u>-</u>
<i>Fund balances:</i>		
Reserved for:		
Encumbrances	77,738	-
New Mexico Business Development Corporation	-	1,363,164
Unreserved:		
Designated for subsequent year's expenditures reported in:		
Debt service	-	-
Arbitrage	-	-
Undesignated, reported in:		
General fund	-	-
<i>Total fund balances</i>	<u>77,738</u>	<u>1,363,164</u>
<i>Total liabilities and fund balances</i>	<u>\$ 324,980</u>	<u>\$ 1,363,164</u>

The accompanying notes are an integral part of these financial statements.

Bond Issuance Fund	General Obligation Bond Funds	Severance Tax Bond Funds	Total Governmental Funds
\$ -	\$ -	\$ -	\$ 324,519
-	47,051,228	106,497,805	153,549,033
-	47,051,228	106,497,805	153,873,552
-	-	-	1,363,164
-	12,089,849	3,210,343	15,300,192
-	-	-	461
-	172,550	6,399	178,949
\$ -	\$ 59,313,627	\$ 109,714,547	\$ 170,716,318
\$ -	\$ -	\$ -	\$ 226,195
-	-	-	21,047
-	-	16,318,268	16,318,268
-	-	84,968	84,968
-	-	16,403,236	16,650,478
-	-	-	77,738
-	-	-	1,363,164
-	58,139,613	90,428,795	148,568,408
-	1,174,014	2,882,516	4,056,530
-	-	-	-
-	59,313,627	93,311,311	154,065,840
\$ -	\$ 59,313,627	\$ 109,714,547	\$ 170,716,318

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STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
GOVERNMENTAL FUNDS

Exhibit B-1
(Page 2 of 2)

RECONCILIATION OF THE BALANCE SHEET TO THE STATEMENT OF NET ASSETS
June 30, 2004

Amounts reported for governmental activities in the statement of
net assets are different because:

Fund balances - total governmental funds	\$ 154,065,840
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	142,432
Compensated absences are not due and payable in the current period and therefore are not reported in the funds.	<u>(83,614)</u>
Net assets of governmental activities	<u><u>\$ 154,124,658</u></u>

The accompanying notes are an integral part of these financial statements.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
For the year ended June 30, 2004

	General	NM Business Development Corp. Fund
<i>Revenues:</i>		
Federal funds	\$ 40,333	\$ -
State general fund appropriations	3,351,800	-
Interest income	-	6,784
Interest income - debt service	-	-
Interest income - arbitrage	-	-
Miscellaneous	-	-
<i>Total revenues</i>	<u>3,392,133</u>	<u>6,784</u>
<i>Expenditures:</i>		
Current:		
Personnel services and employee benefits	2,250,800	-
Operating costs	613,849	-
Contractual services	154,168	19,774
Other administrative expenditures	-	-
Capital outlay	178,381	-
Debt service:		
Principal and interest on long-term debt	-	-
Other charges	-	-
<i>Total expenditures</i>	<u>3,197,198</u>	<u>19,774</u>
<i>Excess (deficiency) of revenues over (under) expenditures</i>	<u>194,935</u>	<u>(12,990)</u>
<i>Other financing sources (uses):</i>		
Operating transfers in (out)		
Reversions	(21,047)	-
State property tax levy	-	-
Severance taxes	-	-
Bond proceeds	-	-
Other taxes	-	-
Capital projects - reversions in	-	-
Other	19,540	(289,021)
Severance tax permanent fund - reversions out	-	-
Transfer to other state agency	-	-
<i>Total other financing sources (uses)</i>	<u>(1,507)</u>	<u>(289,021)</u>
<i>Net change in fund balances</i>	193,428	(302,011)
<i>Fund balances - beginning of year</i>	(115,690)	1,665,175
<i>Fund balances - end of year</i>	<u>\$ 77,738</u>	<u>\$ 1,363,164</u>

The accompanying notes are an integral part of these financial statements.

Bond Issuance Fund	General Obligation Bond Funds	Severance Tax Bond Funds	Total Governmental Funds
\$ -	\$ -	\$ -	\$ 40,333
-	-	-	3,351,800
-	-	-	6,784
-	3,263,546	10,284,893	13,548,439
-	94,222	32,586	126,808
-	-	-	-
-	3,357,768	10,317,479	17,074,164
-	-	-	2,250,800
-	-	-	613,849
-	-	-	173,942
-	-	-	-
-	-	-	178,381
-	53,441,763	325,539,130	378,980,893
-	2,106,615	713,432	2,820,047
-	55,548,378	326,252,562	385,017,912
-	(52,190,610)	(315,935,083)	(367,943,748)
-	-	-	(21,047)
-	52,192,007	-	52,192,007
-	-	311,007,941	311,007,941
86,430,000	-	14,554	86,444,554
-	732,270	-	732,270
-	722,079	2,790,483	3,512,562
-	-	-	(269,481)
-	-	(16,318,268)	(16,318,268)
(86,430,000)	-	-	(86,430,000)
-	53,646,356	297,494,710	350,850,538
-	1,455,746	(18,440,373)	(17,093,210)
-	57,857,881	111,751,684	171,159,050
\$ -	\$ 59,313,627	\$ 93,311,311	\$ 154,065,840

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STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
For the year ended June 30, 2004

Exhibit B-2
(Page 2 of 2)

Amounts reported for governmental activities in the statement of activities
are different because:

Net change in fund balances - total governmental funds	\$ (17,093,210)
--	-----------------

Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.	(26,215)
---	----------

Governmental funds report payments of compensated absences as expenditures. However, changes in the accrued balances of compensated absences are reported in the statement of activities.	<u>(16,300)</u>
---	-----------------

Change in net assets of governmental activities	<u><u>\$ (17,135,725)</u></u>
---	-------------------------------

The accompanying notes are an integral part of these financial statements.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
STATEMENT OF REVENUES AND EXPENDITURES - BUDGET (NON-GAAP)
BASIS AND ACTUAL - GENERAL FUND
Year Ended June 30, 2004

	Budgeted Amounts	
	Original	Final
<i>Revenues:</i>		
State General Fund appropriation	\$ 3,351,800	\$ 3,351,800
Other grants	35,800	35,800
Other financing sources	28,900	113,017
<i>Total revenues</i>	<u>\$ 3,416,500</u>	<u>\$ 3,500,617</u>

	Budgeted Amounts		Expenditures	Outstanding Encumbrances
	Original	Final		
<i>Expenditures:</i>				
Current:				
Personnel services and benefits	\$ 2,505,700	\$ 2,252,700	\$ 2,250,800	\$ -
Contractual services	178,300	178,300	97,581	80,719
Operating costs	648,383	985,500	759,409	215,459
<i>Total expenditures</i>	<u>3,332,383</u>	<u>3,416,500</u>	<u>3,107,790</u>	<u>296,178</u>
<i>Other financing uses</i>	<u>84,117</u>	<u>84,117</u>	<u>84,117</u>	<u>-</u>
<i>Total expenditures and other financing uses</i>	<u>\$ 3,416,500</u>	<u>\$ 3,500,617</u>	<u>\$ 3,191,907</u>	<u>\$ 296,178</u>

The accompanying notes are an integral part of these financial statements.

<u>Actual Amounts</u>	<u>Variance with Final Budget- Favorable (Unfavorable)</u>
\$ 3,351,800	\$ -
40,333	4,533
113,017	-
<u>\$ 3,505,150</u>	<u>\$ 4,533</u>

<u>Total Actual Amounts</u>	<u>Variance with Final Budget- Favorable (Unfavorable)</u>
\$ 2,250,800	\$ 1,900
178,300	-
974,868	10,632
<u>3,403,968</u>	<u>12,532</u>
<u>84,117</u>	<u>-</u>
<u>\$ 3,488,085</u>	<u>\$ 12,532</u>

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
STATEMENT OF FIDUCIARY NET ASSETS
June 30, 2004

Exhibit D-1

	<u>Investment Trust Fund</u>
ASSETS	
<i>Cash and Investments:</i>	
Cash and cash equivalents	\$ 32,365,441
Certificates of deposit	232,950,000
U.S. Government securities	858,982,978
Corporate Bonds	29,216,255
Repurchase agreements	<u>2,779,824,521</u>
<i>Total Cash and Investments</i>	3,933,339,195
<i>Other Assets:</i>	
Accrued interest receivable	<u>5,287,526</u>
<i>Total Assets</i>	<u><u>\$ 3,938,626,721</u></u>
 LIABILITIES AND FUND EQUITY	
<i>Liabilities:</i>	
<i>Fund equity:</i>	
Fund balances, unreserved:	
Net assets held in trust	<u>\$ 3,938,626,721</u>
<i>Total fund equity and net assets held in trust</i>	<u>3,938,626,721</u>
<i>Total liabilities and fund equity and net assets held in trust</i>	<u><u>\$ 3,938,626,721</u></u>

The accompanying notes are an integral part of these financial statements.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
For the Year Ended June 30, 2004

Exhibit D-2

	<u>Investment Trust Fund</u>
Investment Income	\$ 75,946,202
Expenses - Management Fees	<u>(396,020)</u>
Net Investment Income	75,550,182
Net proceeds of deposits (withdrawals)	362,017,161
Net Assets, held in trust for pool participants, June 30, 2003	<u>3,501,059,378</u>
Net Assets, held in trust for pool participants, June 30, 2004	<u><u>\$ 3,938,626,721</u></u>

The accompanying notes are an integral part of these financial statements.

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STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies

The Office of the State Treasurer (State Treasurer) has existed continuously since 1851 (Laws 1851-1852). The Legislative Assembly of the Territory of New Mexico passed an act to establish and regulate the Treasury Department of the Territory of New Mexico. This act established the office of territorial Treasurer and designed the duties of Treasurer.

The Office of the State Treasurer is established by the New Mexico Constitution, Article V, Section 1, which provides in part:

The executive department shall consist of a governor, lieutenant governor, secretary of state, state auditor, state treasurer, attorney general, and commissioner of public lands, who shall, unless otherwise provided in the constitution of New Mexico, be elected for the term of four years beginning on the first day of January next after their election. The governor and lieutenant governor shall be elected jointly by the casting by each voter of a single vote applicable to both offices.

Statutory powers and duties of the State Treasurer are contained in numerous articles of the New Mexico Statutes Annotated. Principal statutory provisions related to the New Mexico State Treasurer's Investment Fund are listed below:

- (1) Sections 8-6-1 through 8-6-7 NMSA 1978 (1983 Repl.), as amended. Section 8-6-3 NMSA 1978 (1983 Repl.) provides that the State Treasurer shall receive and keep all monies of the state, except when otherwise provided, shall disburse the public money upon lawful warrants and shall keep a just, true and comprehensive account of all monies received and disbursed.
- (2) Section 6-1-13 NMSA 1978 (1978 Repl.) provides that the State Treasurer shall authorize all state agency deposit accounts and shall establish conditions and reports appropriate to the accounts.
- (3) Section 6-8-2 NMSA 1978 (1988 Repl.) provides that the State Treasurer shall be a member of the State Investment Council. Section 6-8-6 NMSA 1978 (1988 Repl.) states that the State Treasurer shall maintain custody of the state permanent fund.
- (4) Sections 6-10-11 (G), (H), and (I) NMSA 1978 (1988 Supp.) empower the State Treasurer, with the advice and consent of the State Board of Finance, to invest money held in demand deposits and not immediately needed for the operation of state government in certain specified securities or investments.
- (5) Section 12-6-4 NMSA 1978 provides that the cost of the annual audit of the State Treasurer shall be borne by special appropriations to the State Board of Finance. The cost of the audit and other expenses paid in behalf to the New Mexico State Treasurer's Investment Fund not material to the combined financial statements are not reflected in the accompanying financial statements.
- (6) Section 6-124-2 NMSA 1978 is to ensure an orderly and uninterrupted flow of money to the general fund by anticipating the receipt of taxes and other state revenue.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies (continued)

- (7) Section 61-10-10.1 Short-term investment fund created; distribution of earnings; report of investment.
- a. There is created in the state treasury the "short-term investment fund". The fund shall consist of all deposits from governmental entities and Indian tribes or pueblos that are placed in the custody of the State Treasurer for short-term investment purposes pursuant to this section. The State Treasurer shall maintain a separate account for each governmental entity and Indian tribe or pueblo having deposits in the fund.
 - b. If any local public body is unable to receive payment on public money at the rate of interest as set forth in Section 6-10-36 NMSA 1978 from financial institutions within the geographic boundaries of the governmental unit, then a local public finance official having money of that local public body in his custody required for expenditure within thirty days or less may, with the consent of the appropriate local board of finance, if any, remit some or all of such money to the state treasurer, bank, savings and loan association or credit union for deposit for the purpose of short-term investment as allowed by this section.
 - c. Before any local funds are invested or reinvested for the purpose of short-term investment pursuant to this section, the local public body finance official shall notify and make sure funds are made available to banks, savings and loan associations and credit unions located within the geographical boundaries of their respective governmental unit, subject to the limitation on credit union accounts. To be eligible for such funds, the financial institution shall pay to the local public body the rate established by the State Treasurer pursuant to a policy adopted by the State Board of Finance for such short-term investments.
 - d. The local public body finance official shall specify the length of time each deposit shall be in the short-term investment fund, but in any event the deposit shall not be made for more than thirty days. The State Treasurer through the use of the state fiscal agent shall separately track each such deposit and shall make such information available to the public upon written request.
 - e. The State Treasurer shall invest the fund as provided for state funds under Section 6-10-10 NMSA 1978 and may elect to have the short-term investment fund consolidated for investment purposes with the state funds under the control of the State Treasurer; provided that accurate and detailed accounting records are maintained for the account of each participating entity and Indian tribe or pueblo and that a proportionate amount of interest earned is credited to each of the separate government accounts. The fund shall be invested to achieve its objective, which is to realize the maximum return consistent with safe and prudent management.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies (continued)

f. At the end of each month, all interest earned from investment of the short-term investment fund shall be distributed by the State Treasurer to the contributing entities and Indian tribes or pueblos in amounts directly proportionate to the respective amounts deposited in the fund and the length of time the amounts in the fund were invested. No fees or transfer expenses shall be charged to the participating entities and Indian tribes or pueblos for investment in the short-term investment fund.

The Office of the State Treasurer is responsible for making the State of New Mexico's debt service and interest payments on general obligation and severance tax bonds and maintaining the related accounting records. The proceeds from the issuance of these general obligation and severance tax bonds and the related debt are maintained in funds at the Department of Finance and Administration (DFA) and are not part of this audit. Those funds are included in the DFA's financial statements. The debt service activity and ending balances for the general obligation and severance tax bonds is included in the Supplementary Information section of this report and the statewide CAFR.

Certain investments owned and administered by the Department of Highway and Transportation are purchased through the State Treasurer's Office. The fair value and other gratuitous information related to these investments are not included in the financial statements of the Investment Trust Fund.

The State Treasurer's Office operates several investment pools which collectively represent the cash and investments held at the State Treasurer's Office. These pools represent amounts being held and invested for state agencies and for local governments. They have been identified as 1) state funds investment pool, 2) short-term investment pool, and 3) consolidated investment pool.

Oversight by the State Board of Finance

The State Board of Finance (Board), by statute is comprised of the State of New Mexico governor, lieutenant governor, state treasurer and four members from the general public, and each is a voting member of the Board.

The Board has the responsibility for the issuance of the general obligation and severance tax bonds and for the investment and distribution of the proceeds from such bonds. In that regard, the Board approves the issuance of all such bonds, and provides information for bond prospectuses in order to ensure compliance with financial disclosure requirements and to present information concerning bond issues in a meaningful and informative format. Bonds issued by the Board and the corresponding debt service funds are accounted for by the Office of the State Treasurer and are included in the accompanying financial statements.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies (continued)

Financial Reporting Entity

The Office of the State Treasurer is a department of the State of New Mexico. The financial statements and notes to the financial statements include all funds for which the State Treasurer is responsible. These financial statements only present activity related to the Treasurers Office. The State Treasurer receives funding from state and federal sources and must comply with the requirements of these funding source entities. However, the State Treasurer is not included in any other governmental "reporting entity" as defined by GASB pronouncements, since the State Treasurer is elected by the public and have decision making authority, the power to designate management, the ability to significantly influence operations and have primary financial accountability for fiscal matters. In addition, there are no component units as defined in Governmental Accounting Standards Board Statement 14, which are included in the State Treasurer's reporting entity.

Government-wide and fund financial statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the government. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

As discussed in Note 19 to the financial statements, the Office of the State Treasurer and the Department of Finance and Administration evaluated financial statement reporting issues related to long-term debt obligations. In previous years, the Office of the State Treasurer reported the State of New Mexico's bond obligations as long-term debt on its government-wide statement of net assets. Since the State of New Mexico, not the Office of the State Treasurer, is obligated for the actual debt, the long-term debt obligations of the State of New Mexico have been removed from the Office of the State Treasurer's government-wide statement of net assets, and will be included in the Department of Finance and Administration's financial statements as an agency fund. A decision was made to include debt service activity in the Office of the State Treasurer's financial statements since the Office of the State Treasurer is responsible, by statute, for making debt service payments on behalf of the State of New Mexico. Accordingly, the debt service activity reported in the Statement of Activities of the Office of the State Treasurer and in the Agency Fund reported in the financial statements of the Department of Finance and Administration will be eliminated during the preparation of the State of New Mexico's Statewide Comprehensive Annual Report (CAFR) and the long-term debt obligations of the State of New Mexico will be reported as part of the Statement of Net Assets in the CAFR. As a result, the June 30, 2003 ending net assets presented in the government-wide statement of net assets of the Office of the State Treasurer have been increased \$761,104,004 to reflect the changes discussed above.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies (continued)

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate financial statements are provided for governmental funds and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds are reported as separate columns in the fund financial statements.

Measurement focus, basis of accounting, and financial statement presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are billed.

Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies (continued)

Measurement focus, basis of accounting, and financial statement presentation (continued)

Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The government reports the following major governmental funds:

The *General Fund* is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The *New Mexico Business Development Corporation Fund* was established to account for the State's investment in the New Mexico Business Development Corporation Bank. The authority for the creation of the fund was Sections 53-7-18 through 53-7-46 NMSA 1978.

The *Bond Issuance Fund* was established to account for the issuance and related issuance costs of severance tax and general obligation bond issues. The corresponding debt is accounted for in the *General Obligation Bond Funds* and the *Severance Tax Bond Funds*.

The *General Obligation Bond Funds* are to account for payment of principal and interest on general obligation bonds. Financing sources are provided through the collection of property tax levies levied by other state agencies.

The *Severance Tax Bond Funds* are to account for tax receipts levied by other state agencies upon natural resource products, severed and saved from the lands of the State of New Mexico and to account for payment of principal and interest on severance tax bonds.

Additionally, the government reports the following fiduciary fund types:

The *Short-Term Investment Pool* accounts for cash, securities and other investments identified and held in custody only for the Local Government Investment Pool (LGIP).

The *Consolidated Investment Pool* accounts for cash, short-term securities and other investments held in custody for both state and local government agencies.

The *State Funds Investment Pool* accounts for cash, securities and other investments, identified and held in custody only for state agencies.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies (continued)

Measurement focus, basis of accounting, and financial statement presentation (continued)

Amounts reported as *program revenues* include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes.

The effect of interfund activity has been eliminated from the government-wide financial statements.

Assets, Liabilities and Net Assets or Equity

Deposits and Investments: The State Treasurer's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

State statutes authorize the State Treasurer to invest in, subject to various restrictions, U.S. government obligations, commercial paper, corporate bonds, asset backed obligations, repurchase agreements, certificates of deposit, securities lending transactions, variable rate notes, tax-exempt securities, and money market mutual funds.

Receivables and Payables: Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible. In the government-wide and governmental fund financial statements, delinquent property taxes are not recorded as revenue until received.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies (continued)

Assets, Liabilities and Net Assets or Equity (continued)

Capital Assets: Capital assets, which include equipment, are reported in the applicable governmental columns in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$1,000 (amount not rounded) and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. Information Technology Equipment including software is being capitalized and included in furniture, fixtures and equipment in accordance with NMAC 2.20.1.9 C (5) and *AICPA Statement of Position 98-1*.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

Equipment of the State Treasurer is depreciated using the straight line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Office equipment	5
Computer equipment	5

Compensated Absences: Employees are entitled to accumulate annual leave at the rate based on appointment date and length of continuous services. A maximum of 240 hours of such accumulated annual leave may be carried forward after the pay period beginning in December and ending in January. When employees terminate, they are compensated for accumulated unpaid annual leave as of the date of termination, up to a maximum of 240 hours.

Employees are entitled to accumulate sick leave at the rate of 3.69 hours per pay period. There is no limit to the amount of sick leave which an employee may accumulate. State agencies are allowed to pay fifty (50) percent of each employee's hourly rate for accumulated sick leave over 600 hours up to 120 hours. Payment may be made only once per fiscal year at an employee specified pay period in either January or July.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 1. Summary of Significant Accounting Policies (continued)

Long-term Obligations: In the government-wide financial statements, long-term debt and other long-term obligations are not reported as liabilities in the applicable governmental activities. The Office of the State Treasurer is not the issuer of the debt, nor is it ultimately responsible for the debt. As described more fully in Note 19, long-term debt is reported in the Supplementary Information section of the financial statement. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method and are reported as Supplementary Information in Schedule 6 of the financial statements. Bonds payable are reported net of the applicable bond premium or discount in Schedule 6.

As more fully described in Note 19, the Office reports the debt service activity of the State of New Mexico in its fund financial statements. Governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Fiduciary Net Assets: The combining statement of changes in fiduciary net assets reports the deposits and withdrawals made by the participants in the Investment Trust Funds as "net deposits and withdrawals". These amounts are reported as net, rather than gross, due to the volume of transactions completed during a fiscal period.

Fund Equity: In the fund financial statements, governmental funds report reservations of fund balance that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Restricted Resources: When the Office of the State Treasurer has both restricted and unrestricted resources available to finance a particular program, it is the Government's policy to use restricted resources before unrestricted resources.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 2. Stewardship, Compliance and Accountability

Budgets and Budgetary Accounting

The State Treasurer follows these procedures in establishing the budgetary data reflected in the financial statements:

1. By September 1st, the State Treasurer prepares a budget appropriation request by category to be presented to the next legislature.
2. The appropriation request is submitted to the Department of Finance and Administration's Budget Division (DFA) and to the Legislative Finance Committee (LFC).
3. DFA makes recommendations and adjustments to the appropriation request which become the Governor's proposal to the Legislature.
4. LFC holds hearings on the appropriation request, also submitting recommendations and adjustments before presentation to the Legislature.
5. Both DFA's and LFC's recommended appropriation proposals are presented to the Legislature for approval of the final budget plan.
6. Budgetary control is exercised at the category level of the State Treasurer as a whole and changes are approved by the DFA.
7. Formal budgetary integration is employed as a management control device during the year for the General Fund.
8. The budget for the General Fund is adopted on a cash encumbrances basis. Current year encumbrances are included as expenditures and payment of prior year encumbrances is excluded from expenditures. There is no recognition of changes in prepaid expenses, accounts payable and property, plant and equipment. Budgetary comparisons presented for the General Fund in the report are on the non-GAAP budgetary basis, which does not conform to accounting principles generally accepted in the United States of America because encumbrances are treated as expenditures; increases to expenditures to be funded from fund balances do not cause a corresponding increase in revenues; and this procedure conforms to DFA and State requirements.
9. The State Treasurer's budget for the fiscal year ending June 30, 2004 was amended in a legally permissible manner by reallocating line item category totals as the need arose during the fiscal year. Individual amendments were not material in relation to the original budget.

The New Mexico Business Development Corporation Special Revenue Fund and the Bond Issuance Fund are not budgeted. Debt Service funds are budgeted over the life of their respective bond issues and not on an annual basis.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 2. Stewardship, Compliance and Accountability (continued)

Budgets and Budgetary Accounting (continued)

The following is a reconciliation between the Non-GAAP budgetary (cash) basis amounts and the governmental fund financial statements by fund type.

	General Fund
Excess (deficiency) of revenues over expenditures	\$ 194,935
Adjustments:	
Accounts payable	(20,935)
2004 outstanding encumbrances	(296,178)
2003 encumbrance transactions	126,458
Reversions	(16,115)
Budgeted other financing sources and uses	<u>28,900</u>
Excess (deficiency) of revenues over expenditures (Budget Basis)	\$ <u>17,065</u>

NOTE 3. Deposits and Investments

Fiscal Agent Bank: The State Board of Finance and Wells Fargo Bank in Albuquerque (Bank) entered into an agreement whereby the Bank would provide banking services as Fiscal Agent for the State of New Mexico through September 30, 2005 with the option to renew for two additional years at the option of the State Board of Finance.

Correspondent Bank: The State Board of Finance and Northern Trust entered into an agreement whereby BTC would provide banking services as Correspondent Bank for the State of New Mexico through September 30, 2005 with the option to renew for two additional years at the option of the State Board of Finance.

The following funds are included in cash and investments of the Office of the State Treasurer:

Account Description	CAS Fund #	Amount
General	182	\$ <u>324,519</u>
Investment Trust Fund	N/A	\$ <u>265,315,441</u>

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 3. Deposits and Investments (continued)

<u>Account Description</u>	<u>CAS Fund #</u>	<u>Amount</u>
Debt Service Funds:		
General Obligation and Revenue Bonds:		
1999 General Obligation Debt Service	640	8,849,815
1999 General Obligation Debt Service – Rebate Excess Earnings	409	465,406
2000 Enhanced 911 Revenue	018	711,570
2000 Enhanced 911 Revenue – Rebate Excess Earnings	488	86,193
2001 General Obligation Debt Service	414	6,720,387
2001-A General Obligation Debt Service – Rebate Excess Earnings	415	611,539
2001-A General Obligation Debt Service – Rebate Excess Earnings	712	2,748
2001-A General Obligation Debt Service	487	7,858,000
2001-B General Obligation Debt Service -- Refunding	482	6,571,655
2003 General Obligation Debt Service	031	13,929,483
2003-B General Obligation Debt Service -- Refunding	418	1,244,432
		<u>47,051,228</u>
Severance Tax Bonds		
Severance Tax Bonding Fund	410	18,411,295
1999-A Supplemental Severance Tax Debt Service	184	1,945,820
1999-A Supplemental Severance Tax Debt Service – Rebate Excess Earnings	185	228,967
1999-B Series Debt Service	186	5,550,744
1999-B Severance Tax Debt Service – Rebate Excess Earnings	461	1,194,601
2000 Severance Tax Debt Service – Rebate Excess Earnings	391	1,249,650
2000 Severance Tax Debt Service	389	12,277,033
2000-C Series Rebate	406	294,150
2000-C Series Debt Service	405	2,044,452
2001-A Severance Tax Debt Service	408	15,559,679
2002-A Series Debt Service	699	8,386,714
2002-A Severance Tax Debt Service	095	8,439,010
2002-B Supplemental Series – Debt Service	390	5,329,291
2003-A Series – Debt Service	884	24,599,409
2003-B Series – Debt Service	484	952,101
2004-A Series – Debt Service	492	34,889
		<u>106,497,805</u>
Total Debt Service		153,549,033
Investment Trust Fund	N/A	<u>2,779,824,521</u>
Total Repurchase Agreements		<u>\$ 2,933,373,554</u>

Investment Trust Fund

Cash on deposit represents the demand deposit account with the fiscal agent bank. Current year transactions reflect all banking activity for the fiscal year as well as the activity of investments purchased and disposed of during the fiscal year.

The State Treasurer does not hold cash in the office vault. All amounts deposited with the State Treasurer are subsequently redeposited in the fiscal agent account or invested in certificates of deposit, treasury securities or overnight repurchase agreements.

The State Treasurer invests all public monies held in excess of the minimum compensating balance maintained with the fiscal agent bank in accordance with an investment policy approved by the State Board of Finance.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 3. Deposits and Investments (continued)

Investment Trust Fund (continued)

The Treasurer's Investment Trust Fund has implemented GASB Statement No. 31 "Accounting and Financial Reporting for Certain Investments". This statement requires that certain investments as defined in GASB Statement No. 31 to be valued at fair value. Fair value is based on quoted market prices as of the valuation date. The change in fair value is recognized as a component of investment income in the current year.

The State Treasurer invests excess cash balances on behalf of certain earmarked funds of state agencies identified by state statute and local governments. Interest earnings are distributed based on average outstanding cash balances for local governments and the state agencies where interest is allowed to be earned. All other interest earnings are transferred to the State General Fund.

The Treasurer's Investment Trust Fund does not participate in securities lending transactions.

The State Treasurer deposits public monies with New Mexico financial institutions in denominations which generally are in excess of the \$100,000 in insurance coverage provided by federal agencies. Accordingly, the State Treasurer requires that depository financial institutions provide additional collateral for such investments. The collateral generally is in the form of marketable debt securities and is required in amounts ranging from 50% to 102% of the par value of the investment dependent upon the institutions operating results and capital. Collateral for the fiscal agent account is required in amounts equal to 50% of the average investment balance. At June 30, 2004 collateral pledged to public money deposits was as follows:

	Fiscal Agent Account	Certificates Of Deposit	Total
Cash in bank	\$ 165,416,609	\$ 232,950,000	\$ 398,366,609
Less FDIC insurance coverage	<u>(100,000)</u>	<u>(2,800,000)</u>	<u>(2,900,000)</u>
Total unsecured public funds	<u>\$ 165,316,609</u>	<u>\$ 230,150,000</u>	<u>\$ 395,466,609</u>
Collateral requirement (50% of uninsured public funds)	\$ 82,658,304	\$ 115,075,000	\$ 197,733,304
Collateral pledged: US Government securities	<u>(97,544,235)</u>	<u>(144,084,955)</u>	<u>(241,629,190)</u>
(Over) Under Collateralized	<u>\$ (14,885,931)</u>	<u>\$ (29,009,955)</u>	<u>\$ (43,895,886)</u>

STATE OF NEW MEXICO
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Notes to Financial Statements
June 30, 2004

NOTE 3. Deposits and Investments (continued)

The statutes of the State of New Mexico place certain restrictions on the investments of public money by the State Treasurer in order to minimize risk. Permissible investments include U.S. Treasury securities and certificates of deposit at financial institutions insured by an agency of the federal government and corporate bonds that meet the investment policy criteria. In order to meet short-term investment objectives, state laws permit investment in repurchase agreements. These contracts must be fully secured by obligations of the United States or other securities backed by the United States, having a market value of at least 102% of the amount of the contract.

In accordance with GASB Statement No. 3, investments must be categorized to give an indication of the level of risk assumed by the State at year-end. **Category 1** includes investments that are insured or registered or for which the securities are held by the State Treasurer or agent in the Office's name. **Category 2** includes uninsured and unregistered investments for which the securities are held by the broker's or dealer's trust department or agent in the Office's name. **Category 3** includes uninsured or unregistered investments for which the securities are held by the broker or dealer, or by its trust department or agent, but not in the Office's name. All of the investments at June 30, 2004 are Category 2 investments.

At June 30, 2004, investments in repurchase agreements were \$2,933,373,554. Collateral required by State statute at June 30, 2004 was \$2,992,041,025. The investments in repurchase agreements were collateralized by U.S. Treasury notes and bills valued at \$3,019,363,254 held at Northern Trust Company in California, in the Office's name. Fair value for the securities below was obtained from Northern Trust Company in California and reflects quoted market prices as of June 30, 2004.

Investments administered by the State Treasurer at June 30, 2004 include the following:

Description	Amortized Cost	Carrying Amount Fair Value
US Government securities	\$ 866,077,525	\$ 858,982,978
Corporate bonds	29,488,974	29,216,255
Repurchase agreements	<u>2,933,373,554</u>	<u>2,933,373,554</u>
	<u>\$ 3,828,940,053</u>	<u>\$ 3,821,572,787</u>

Funds whose investments are debt related record no investment earnings. These earnings are recorded in the appropriate debt service funds.

STATE OF NEW MEXICO
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Notes to Financial Statements
June 30, 2004

NOTE 3. Deposits and Investments (continued)

The State Treasurer also administers an investment of \$1,363,164 in New Mexico Business Development Corporation bonds on behalf of the State of New Mexico. The original bond investment of \$2,528,332 was called in October 1991 (See Note 11). This investment is reflected in the New Mexico Business Development Corporation Special Revenue Fund.

The book value and other gratuitous information related to the custodial investments are not included in the financial statements of the Office of the State Treasurer.

Local Government Investment Pool: Cities, counties, and other non-state agencies invest monies in the State Treasurer external investment pool (Local Government Investment Pool). The investments are recorded at fair value based on quoted market prices as of the valuation date in the financial statements, however, the individual participant balances remain at their carrying cost. At June 30, 2004 the carrying cost and the fair value were the same in the Local Government Investment Pool.

The State Treasurer Local Government Investment Pool is not SEC registered. Section 6-10-10 I, NMSA 1978, empowers the State Treasurer, with the advice and consent of the State Board of Finance, to invest money held in the short-term investment fund in securities that are issued by the United States government or by its departments or agencies and are either direct obligations of the United States or are backed by the full faith and credit of the United States government or are agencies sponsored by the United States government. The Local Government Investment Pool investments are monitored by the same investment committee and the same policies and procedures that apply to all other state investments.

The pool does not have unit shares. Per Section 6-10-10.1F, NMSA 1978, at the end of each month all interest earned is distributed by the State Treasurer to the contributing entities in amounts directly proportionate to the respective amounts deposited in the fund and the length of time the amounts were invested.

Participation in the local government investment pool is voluntary.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 4. Capital Assets

Capital asset activity for the year ended June 30, 2004 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Governmental activities:				
Capital assets, being depreciated				
Equipment	\$ 291,364	\$ 36,284	(3,000)	\$ 324,648
Total capital assets being depreciated	291,364	36,284	(3,000)	324,648
Less accumulated depreciation for:				
Equipment	(122,717)	(60,049)	550	(182,216)
Total accumulated depreciation	(122,717)	(60,049)	550	(182,216)
Total capital assets being depreciated, net	\$ 168,647	\$ (23,765)	\$ (2,450)	\$ 142,432

Depreciation expense was charged to functions/programs of the Office as follows:

Governmental activities:	
General government	\$ 60,049
Total depreciation expense – governmental activities	\$ 60,049

NOTE 5. Long-Term Obligations

Compensated Absences

As in prior years, the general fund is used to liquidate compensated absences. Following are the changes in compensated absences for the year ended December 31, 2004:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated absences	\$ 67,314	\$ 90,572	\$ 74,272	\$ 83,614	\$ 74,000

Additional Information Related to Long-Term Debt Obligations of the State of New Mexico

As discussed in Note 19 to the financial statements, the long-term debt obligations of the State of New Mexico have been removed from the Statement of Net Assets of the Office of the State Treasurer. However, information regarding the long-term debt obligations of the State of New Mexico and the related debt service requirements has been incorporated into this report as Schedule 6 – Summary of Long-Term Debt Obligations to assist the State of New Mexico in preparing the Statewide Comprehensive Annual Report.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 6. Condensed Financial Statements

Condensed financial statements of the Investment Trust Fund, inclusive of external and internal participants for the fiscal year ended June 30, 2004, are as follows:

State Treasurer's Investment Trust Fund
Balance Sheet
June 30, 2004

Assets

Cash and Cash Equivalents	\$ 32,365,441
Investments	3,900,973,754
Interest Receivable	<u>5,287,526</u>
Total Assets	<u>\$ 3,938,626,721</u>

Liabilities and Net Assets:

External Participant account balances	\$ 1,261,644,750
Other Internal Participant account balances	
Primary Government	2,684,349,236
Undistributed Reserves and Unrealized Gains (Losses)	<u>(7,367,265)</u>
Total Net Assets	<u>\$ 3,938,626,721</u>

Investment Income – At June 30, 2004 the Office's investment income earnings were as follows:

Local Government Investment Pool	\$ 22,630,062
Consolidated Investment Pool	16,907,847
Short-term Investment Pool	43,775,558
Unrealized Loss	<u>(7,367,265)</u>
	<u>\$ 75,946,202</u>

NOTE 7. Appropriations and Other Revenue

The Office received the following appropriations and other revenue for the year ended June 30, 2004:

General Fund	
General appropriation, (General Appropriation Act)	\$ 3,183,500
Special appropriation	<u>168,300</u>
Total state general fund appropriations	<u>\$ 3,351,800</u>

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 8. Collateral in Trust

The State Treasurer holds a variety of different types of collateral, government guaranteed loans and mortgages, certificates of deposit, surety bonds, etc., for certain state agencies, which are not included in the financial statements.

NOTE 9. Due to Severance Tax Permanent Fund and Reversions

The State Treasurer is required by statute (Section 7-27-8 NMSA 1978, 1986 Repl.) to transfer to the Severance Tax Permanent Fund, all monies in the Severance Tax Bonding Fund, except the amount necessary to meet principal and interest payments on bonds payable of the next two ensuing semi-annual payment dates. A balance of \$16,318,268 remains in the Severance Tax Bonding Fund payable to the Severance Tax Permanent Fund that was transferred in July 2004.

NOTE 10. Arbitrage on Tax Exempt Bonds

Prior to the Tax Reform Act (TRA) of 1986, state and local governments had up to three years to use the proceeds from tax exempt bonds issued by them before arbitrage on such proceeds had to be paid to the Treasury Department. Arbitrage, as defined, is the excess interest earned by a state or local government on proceeds from the sale of its bonds over interest paid to bond holders.

TRA 1986 required rebate of such arbitrage to the Treasury Department on governmental bonds issued after August 31, 1986, and on private activity bonds issued after December 31, 1984, when the proceeds were held for six months or longer. These rebates must be calculated annually and paid at the end of every fifth year until the bonds are retired.

The Revenue Reconciliation Act of 1989 amended the six-month rule. For bonds issued after December 19, 1989 the rebate requirement does not apply if, both, all of the gross proceeds of the issue, other than the reserve fund, are spent within the six-month period following the date of issue, and the rebate requirement is satisfied for the reserve fund after the six month period. The term gross proceeds for purposes of the rule include both the sale proceeds received from the bond purchase on the issue date and investment earnings on such proceeds during the six-month period. Gross proceeds deposited in a reserve fund or bona fide debt service fund, however, are not subject to the expenditure requirement.

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 10. Arbitrage on Tax Exempt Bonds (continued)

The following is a schedule of bond issues, along with the bond year ends and arbitrage rebate due dates. The State Treasurer's Office has had the first arbitrage computation for the bonds, completed as indicated:

	Bond Year End of First Rebate Computation	First Arbitrage Rebate Due Date	First Computation of Arbitrage Completed
General Obligation Capital Projects Bonds Series 1993	September 1998	November 1998	X
General Obligation Capital Projects Bonds Series 1993B	September 1998	November 1998	X
General Obligation Capital Projects Improvement Bonds Series 1995	September 2000	November 2000	X
General Obligation Capital Projects Improvement Bonds Series 1997	September 2002	November 2002	X
General Obligation Capital Projects Bonds Series 1999	July 2004	August 2004	X
General Obligation Bonds Series 2001	July 2005	August 2005	
General Obligation Bonds Refunding Series 2001A	July 2005	August 2005	
General Obligation Bonds Refunding Series 2001B			
General Obligation Bonds Series 2003			
General Obligation Bonds Refunding Series 2003B			
Severance Tax Bonds Series 1993B	July 1998	August 1998	X
Severance Tax Bonds Series 1994B	July 1999	August 1999	X
Severance Tax Bonds Series 1995A	July 2000	August 2000	X
Severance Tax Bonds Series 1995B	July 2000	August 2000	X
Severance Tax Bonds Series 1996A	July 2001	August 2001	X
Severance Tax Refunding Bonds Series 1997A	July 2002	August 2002	X
Severance Tax Refunding Bonds Series 1998A	July 2003	August 2003	X
Severance Tax Bonds Series 1998B	July 2003	August 2003	X
Severance Tax Bonds Series 1999B	July 2004	August 2004	X
Severance Tax Bonds Series 1999A Supplemental	July 2004	August 2004	
Severance Tax Bonds Series 2000	July 2005	August 2005	
Severance Tax Bonds 2000C Supplemental	July 2006	August 2006	
Severance Tax Bonds Refunding Series 2001A			
Severance Tax Bonds Series 2002A			
Severance Tax Bonds Series 2002A Supplemental			
Severance Tax Bonds Series 2002B Supplemental			
Severance Tax Bonds Series 2003A			
Enhanced 911 Revenue Bonds Series 2000	July 2005	August 2005	

Interest earnings on invested bond proceeds through June 30, 2004 did not exceed the interest costs of the bonds. Such amounts would have been included as a reservation of fund balance in the accompanying financial statements. Amounts due the Internal Revenue Service which are known and measurable are recorded as a liability – accrued arbitrage interest payable in the accompanying financial statements.

STATE OF NEW MEXICO
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Notes to Financial Statements
June 30, 2004

NOTE 11. New Mexico Business Development Corporation (BDC)

In 1991, the State Treasurer called in the original investment of \$2,528,332 in bonds, issued by the BDC to protect the state's share of BDC's assets. This action forced a liquidation of BDC and the remaining assets of BDC were turned over to a trustee, Wells Fargo Bank (formerly Norwest Bank), on behalf of the State Treasurer on October 1, 1991, pursuant to the terms of the "Realization of Assets Agreement." Payment of interest on the remaining outstanding debt ceased as of the call date. Accordingly, no interest income is being accrued in the accompanying financial statements. There are outstanding accounts receivable for BDC, however, since the collectibility is not known, the accounts receivable or corresponding bad debt has not been recognized. The balance at June 30, 2004 is the fair market value at that date.

NOTE 12. Transfers

Bond Proceeds – The Bond Issuance Fund transferred the net proceeds of the General Obligation and Revenue Bonds and Severance Tax Bonds to the Department of Finance and Administration (DFA).

The proceeds were distributed as follows and the proceeds are accounted for in DFA's June 30, 2004 financial statements:

	CFRAS Number	Amount
Severance Tax Bonds – Series 2003 B Supplemental	484	\$ 10,000,000
Severance Tax Bonds – Series 2004 A	492	<u>76,430,000</u>
Total		<u>\$ 86,430,000</u>

Interfund Transfers:

	Fund	Transfer From	Transfer To
Debt Service:			
Severance Tax Bonding Fund	410	\$ 82,666,522	\$ -
Severance Tax Bond – 1998A Debt Service	425	13,281	-
Severance Tax Bond – 1998B Debt Service	411	149,942	-
Severance Tax Bond – 1998A Rebate	486	25,974	-
Severance Tax Bond – 1998B Rebate	426	794,281	-
Severance Tax Bond – 1999A Debt Service	184	-	2,000,000
Severance Tax Bond – 1999B Debt Service	186	-	5,500,000
Severance Tax Bond – 2000 Debt Service	389	-	11,500,000
Severance Tax Bond – 2000C Debt Service	405	-	2,000,000
Severance Tax Bond – 2001A Debt Service	408	-	15,500,000
Severance Tax Bond – 2002A Debt Service	699	-	7,500,000
Severance Tax Bond – 2002A Debt Service	095	-	8,500,000
Severance Tax Bond – 2002B Supplemental Debt Service	390	-	5,200,000
Severance Tax Bond – 2003A Debt Service	884	-	25,100,000
Severance Tax Bond – 2003B Debt Service	484	-	<u>850,000</u>
Total		<u>\$ 83,650,000</u>	<u>\$ 83,650,000</u>

STATE OF NEW MEXICO
OFFICE OF THE STATE TREASURER
Notes to Financial Statements
June 30, 2004

NOTE 13. Employee Retirement Plan – State of New Mexico

Plan Description

Substantially all of the Office's full-time employees participate in a public employee retirement system authorized under the Public Employees Retirement Act (Chapter 10, Article 11 NMSA 1978). The Public Employees Retirement Association (PERA) is the administrator of the plan, which is a cost-sharing multiple-employer defined benefit retirement plan. The plan provides for retirement, disability benefits, survivor benefits and cost-of-living adjustments to plan members and beneficiaries. PERA issues a separate, publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to PERA, P.O. Box 2123, Santa Fe, New Mexico 87504-2123.

Funding Policy

Plan members are required to contribute 7.42% of their gross salary. The Office is required to contribute 16.59% depending upon the division of the gross covered salary. The contribution requirements of plan members and the Office are established under Chapter 10, Article 11 NMSA 1978. The requirements may be amended by acts of the legislature. The Office's contributions to PERA for the years ending June 30, 2004, 2003, and 2002, were \$374,200, \$386,643, and \$390,715, respectively, equal to the amount of the required contributions for each year.

NOTE 14. Post Employment Benefits – Retiree Health Care Act Contributions

The Retiree Health Care Act (Act) (Chapter 10, Article 7C NMSA 1978) provides comprehensive core group health insurance for persons who have retired from certain public service in New Mexico. The Retiree Health Care Authority is the administrator of the plan. The purpose is to provide eligible retirees, their spouses, dependents and surviving spouses and dependents with health insurance consisting of a plan, or optional plans, of benefits that can be purchased by funds flowing into the Retiree Health Care Fund and by co-payments or out-of-pocket payments of eligible retirees.

Monies flow to the Retiree Health Care Fund on a pay-as-you-go basis from eligible employers and eligible retirees. Eligible employers are institutions of higher education, school districts, or other entities participating in the Public School Insurance Authority and state agencies, state courts, magistrate courts, municipalities or counties, which are affiliated under or covered by the Educational Retirement Act, Public Employees Retirement Act, Volunteer Firefighters Retirement Act, Judicial Retirement Act or the Magistrate Retirement Act.

Eligible retirees are: (1) Retirees who made contributions to the fund for at least five years prior to retirement and whose eligible employer during that period of time made contributions as a participant in the Retiree Health Care Act on the person's behalf unless that person retires before the employer's NMRHCA effective date, in which event the time period for contributions shall become the period of time between the employer's effective date and the date of retirement. (2) Retirees defined by the Act who retired prior to July 1, 1990 and former legislators who served at least two years.

STATE OF NEW MEXICO
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Notes to Financial Statements
June 30, 2004

NOTE 14. Post Employment Benefits – Retiree Health Care Act Contributions (continued)

Fund Contributions: Each participating employer makes contributions to the fund in the amount of 1.3 percent of each participating employee's annual salary. Each participating employee contributes to the fund an employee contribution equal to .65 percent of the employee's salary. Each participating retiree pays a monthly premium for the medical plus basic life plan and an additional participation fee of five dollars (\$5.00) if the eligible participant retired prior to the employer's NMRHCA effective date or is a former legislator. Participants may also enroll in optional plans of coverage.

Contributions from participating employers and employees become the property of the Retiree Health Care Fund and are not refundable under any circumstances, including termination of employment or termination of the participating employer's operation or participation in the Retiree Health Care Act. The employer, employee and retiree contributions are required to be remitted to the Retiree Health Care Authority on a monthly basis.

The Retiree Health Care Authority issues a separate, publicly available audited financial report that includes post employment benefit expenditures of premiums and claims paid, participant contributions (employer, employee and retiree) and net expenditures for the fiscal year. The report also includes the approximate number of retirees participating in the plan. That report may be obtained by writing to the Retiree Health Care Authority, 810 West San Mateo, Suite D, Santa Fe, New Mexico 87505.

For the fiscal year ended June 30, 2004, the Office remitted \$19,770 in employer contributions and \$9,885 in employee contributions to the Retiree Health Care Authority.

NOTE 15. Outstanding Encumbrances

The following is a reconciliation of outstanding encumbrances per the Department of Finance and Administration (DFA) Report to the reserve for encumbrances and accounts payable as shown in the financial statements at June 30, 2004:

DFA Report	General Fund
Unadjusted Encumbrances Balance as follows:	
Contractual services	\$ 80,719
Operating costs	149,585
Capital outlay	<u>57,355</u>
	287,659
Adjustments for amounts included in accounts payable	<u>(148,399)</u>
Encumbrances, June 30, 2004	\$ <u>139,260</u>
Reconciliation of fund balance reserved for encumbrances to June 30, 2004 encumbrances:	
June 30, 2004 encumbrances	\$ 139,260
Adjustment for deficit unrestricted fund balance due to accrued expenses recorded using the modified accrual basis of accounting	<u>(61,522)</u>
Fund balance reserved for encumbrances June 30, 2004	\$ <u>77,738</u>

STATE OF NEW MEXICO
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Notes to Financial Statements
June 30, 2004

NOTE 16. Risk Management

The Department is exposed to various risks of loss for which the Department carries insurance (auto; employee fidelity bond; general liability; civil rights and foreign jurisdiction; money and securities; property; and workers' compensation) with the State of New Mexico Risk Management Division. Public employee fidelity bonding coverage is self-insured by the State of New Mexico. The current policy year is July 1, 2003 to June 30, 2004. The limit of coverage is \$5,000,000 with \$1,000 deductible per occurrence. All Office employees are covered by this bond.

NOTE 17. Reversion to the State General Fund

Under State Statute 6-5-10 NMSA, 1978, all unreserved, undesignated fund balances in reverting funds and accounts as reflected in the central accounting system as of June 30, as adjusted, shall revert to the general fund within forty-five days of release of the audit report for that fiscal year.

Amounts expected to revert to the state general fund as of June 30, 2004 are \$21,047, all of which relate to the fiscal year ended June 30, 2004.

Amounts reverted to the State General Fund during 2004 were as follows:

	<u>Appropriation</u>	<u>Reversion</u>
Reversion to State General Fund FY 02	\$ 3,134,200	\$ 6,754
Reversion to State General Fund FY 03	3,183,500	<u>21,047</u>
		\$ <u>27,801</u>

NOTE 18. Deficit Fund Balances and Excess of Expenditures Over Appropriations

Generally accepted accounting principles require disclosures as part of the Combined Statements of certain information concerning individual funds including:

- A. Deficit fund balance of individual funds. No funds experienced deficit fund balances for the year ended June 30, 2004.
- B. Excess of expenditures over appropriations. No funds over expended the appropriations for the year ended June 30, 2004.

NOTE 19. Prior Period Restatement

As discussed in Note 19 to the financial statements, the Office of the State Treasurer and the Department of Finance and Administration evaluated financial statement reporting issues related to long-term debt obligations. In previous years, the Office of the State Treasurer reported the State of New Mexico's bond obligations as long-term debt on its government-wide statement of net assets. Since the State of New Mexico, not the Office of the State Treasurer, is obligated for the actual debt, the long-term debt obligations of the State of New Mexico have been removed from the Office of the State Treasurer's government-wide statement of net assets, and will be included in the Department of Finance and

STATE OF NEW MEXICO
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Notes to Financial Statements
June 30, 2004

NOTE 19. Prior Period Restatement (continued)

Administration's financial statements as an agency fund. A decision was made to include debt service activity in the Office of the State Treasurer's financial statements since the Office of the State Treasurer's financial statements since the Office of the State Treasurer is responsible, by statute, for making debt service payments on behalf of the State of New Mexico. Accordingly, the debt service activity reported in the Statement of Activities of the Office of the State Treasurer and in the Agency Fund reported in the financial statements of the Department of Finance and Administration will be eliminated during the preparation of the State of New Mexico's Statewide Comprehensive Annual Report (CAFR) and the long-term debt obligations of the State of New Mexico will be reported as part of the Statement of Net Assets in the CAFR. As a result, the June 30, 2003 ending net assets presented in the government-wide statement of net assets of the Office of the State Treasurer have been increased \$761,104,004 to reflect the changes discussed above.

NOTE 20. Subsequent Events

Subsequent to June 30, 2004, the State Board of Finance issued the following debt :

Supplemental Severance Tax Bonds, Series 2004B. On November 17, 2004, the State Board of Finance issued \$10,000,000 in bonds to finance public education facilities projects authorized by the State Legislature.

By Statute, the Office of the State Treasurer will be responsible for the debt service activity for these bonds and will record the activity in the Severance Tax Bond Funds of its governmental fund financial statements beginning with the fiscal year ending June 30, 2005. The debt obligation and related activity will be reported by the Department of Finance and Administration in an agency fund beginning June 30, 2005, and the State of New Mexico will report the long-term debt obligation on the statement of net assets of the Statewide Comprehensive Annual Report beginning June 30, 2005.

NOTE 21. Subsequent Accounting Standard Pronouncements

In March 2003, the Governmental Accounting Standards Board (GASB) issued GASB Statement No. 40, *Deposit and Investment Risk Disclosures - an amendment of GASB Statement No. 3*, which is effective for financial statements for periods beginning after June 15, 2004, with earlier application encouraged. The Statement addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of the interest rate risk, this Statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Deposit and investment policies related to the risks identified in this Statement should also be disclosed. The Office of the State Treasurer is analyzing the effect that this standard will have on its financial statements, and currently believes it will have no significant effect on the financial statements for the upcoming year.

STATE OF NEW MEXICO
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June 30, 2004

NOTE 21. Subsequent Accounting Standard Pronouncements (continued)

In November 2003, the Governmental Accounting Standards Board (GASB) issued GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, which is effective for financial statements for periods beginning after December 15, 2004. This statement requires governments to report the effects of capital asset impairments in their financial statements when they occur rather than as part of the ongoing depreciation expense for the capital asset or upon disposal of the capital asset. The Statement also requires all governments to account for insurance recoveries in the same manner. The Office of the State Treasurer is analyzing the effect that this standard will have on its financial statements, and currently believes it will have no significant effect on the financial statements for the upcoming year.

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APPENDIX C

FORM OF ATTORNEY GENERAL'S NO LITIGATION LETTER

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[date]

State Board of Finance
State of New Mexico
Bataan Memorial Bldg., Suite 181
Santa Fe, NM 87501

Sutin Thayer & Browne
A Professional Corporation
P.O. Box 2187
Santa Fe, NM 87504

Brownstein Hyatt & Farber, P.C.
201 Third Street N.W.
Suite 1500
Albuquerque, NM 87102

Re: \$37,040,000 State of New Mexico Severance Tax Bonds, Refunding Series 2005B-1
\$21,095,000 State of New Mexico Supplemental Severance Tax Bonds, Refunding Series 2005B-2

Ladies and Gentlemen:

This letter will serve as our certificate of litigation affecting New Mexico Severance Taxes. The Taxation and Revenue Department ("Department") has settled several cases that were pending at the administrative and judicial levels wherein natural gas producers were challenging the refusal of the Department to reduce the taxable value upon which severance taxes are imposed by certain on-lease expenses, and to refund, with interest, the amounts in controversy. The final case, brought by Marathon, was recently settled.

Additionally, in 2000, the Department assessed a number of taxpayers for additional taxes based upon the taxpayers' under-valuation of oil. Of the four companies who paid the assessments and filed for refunds, one abandoned its refund claim, and the remaining three have settled. In 2001, the Department also assessed a number of taxpayers for additional taxes based upon the taxpayers' under-valuation of natural gas and carbon dioxide. Four taxpayers paid assessments under this program. Two filed for refunds and are currently in litigation with the Department. In one of those cases, the taxpayer was granted summary judgment on a major issue. The Department expects to settle this claim on terms favorable to the taxpayer. In the second case in litigation, the Department was granted summary judgment on a major issue. This matter is currently on appeal and the case is not expected to settle.

Finally, at any given time, a number of protests/refund claims are pending at the administrative level.

As of June 15, 2001 (subsequent to the Department's receipt of payments on assessments discussed above), payments on severance tax assessments issued by the Department, including any on undervaluation assessments made after that date, are held in a suspense fund until the Department Secretary determines that there is no substantial risk of protest or other litigation. See NMSA 1978, § 7-1-6.20(B) (2001).

While we are unable to predict with reasonable certainty the outcome of pending litigation and administrative proceedings, they would not, in our opinion, reasonably be expected to have a material effect on the bondholders.

This office is not aware of any other pending or threatened litigation that would affect the severance tax of the state or the authority of the state to issue these severance tax bonds.

Sincerely,

Assistant Attorney General

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APPENDIX D

**FORM OF OPINION OF BOND COUNSEL
SEVERANCE TAX BONDS, REFUNDING SERIES 2005B-1 and
SUPPLEMENTAL SEVERANCE TAX BONDS, REFUNDING SERIES 2005B-2**

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(Form of Bond Counsel Opinion)

_____, 2005

State Board of Finance
State of New Mexico

Ladies and Gentlemen:

We have examined the transcript of proceedings (the "Transcript") relating to the issuance of \$37,040,000 State of New Mexico Severance Tax Bonds, Refunding Series 2005B-1 (the "Series 2005B-1 Bonds"), dated the date of delivery, and being a series of bonds in registered form maturing on July 1, 2008, and serially thereafter on July 1 of each year through 2012, and the \$21,095,000 State of New Mexico Supplemental Severance Tax Bonds Refunding Series 2005B-2 (the "Series 2005B-2 Bonds") dated the date of delivery, and being a series of bonds in registered form maturing on July 1, 2009, and serially thereafter in July 1 of each year through 2011. The Series 2005B-1 Bonds and the Series 2005B-2 Bonds are collectively referred to herein as the "Bonds".

We have also examined the provisions of the Constitution and laws of the State of New Mexico (the "State") under authority of which the Bonds were issued, the resolution authorizing the issuance and sale of the Bonds (the "Bond Legislation") adopted by the State Board of Finance (the "Board") on May 24, 2005, an executed Bond of the first maturity, and the Tax Certificate of the State (the "Tax Certificate"). We have also made such further inquiries and investigations and have examined such further documents and matters as we have considered necessary in rendering this opinion.

Certain agreements, requirements and procedures contained or referred to in the Bond Legislation, the Tax Certificate and other relevant documents may be changed and certain actions (including, without limitation, the defeasance of Bonds) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. No opinion is expressed herein as to any Bond or the interest thereon with respect to any such change or action taken or omitted upon the advice or approval of counsel other than ourselves.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof. Our engagement with respect to the Bonds has concluded with their issuance, and we disclaim any obligation to update this letter. Furthermore, we have assumed compliance with the covenants and agreements contained in the Bond Legislation and the Tax Certificate, including (without limitation) covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause interest on the Bonds to be included in gross income for federal income tax purposes. We call attention to the fact that the rights and obligations under the Bonds, the Bond Legislation and the Tax Certificate and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to the limitations on legal remedies against the State of New Mexico. We express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum or waiver provisions contained in the documents described herein. Finally, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement or other offering material relating to the Bonds and express herein no opinion relating thereto.

Based on our examination, we are of the opinion that, under the law existing on the date of this opinion:

1. The Bonds constitute valid and binding special obligations of the State in accordance with the terms and provisions thereof.

2. The Bonds are payable solely from, and such payment is secured by a pledge (but not an exclusive pledge) of, the money on deposit in the Severance Tax Bonding Fund (defined in the Bond Legislation), consisting of the net receipts from taxes levied upon certain natural resource products severed and saved from the soil of the State and such other moneys as the State Legislature may, in its sole discretion, from time to time determine to deposit in the Severance Tax Bonding Fund, certain interest earnings on moneys on deposit in the bond accounts and such proceeds of the Bonds as may from time to time be deposited in the Severance Tax Bonding Fund as a result of statutorily required reversions or otherwise; provided, however, that such pledged and any resulting lien of the Series 2005B-2 Bonds is expressly made subordinate to any pledge or lien on such net receipts and other moneys in the Severance Tax Bonding Fund in favor of "Senior Obligations" (as defined in the Bond Legislation) now or hereafter outstanding. Under the Bond Legislation, the Board may also issue additional obligations on a parity with the Bonds on the terms and conditions of the Bond Legislation. The owners of the Bonds have no right to have ad valorem taxes levied by the State for the payment of principal of or interest on the Bonds and the Bonds do not represent or constitute a debt or pledge of, or a charge against, the general credit of the State.

3. The Bond Legislation is valid and binding on the Board, is enforceable in accordance with its terms and creates the pledge which it purports to create.

4. The interest on the Bonds is excludable from gross income for federal income tax purposes under Section 103(a) of the Internal Revenue Code of 1986, as amended (the "Code"), and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, such interest is taken into account in determining adjusted current earnings for the purpose of computing the alternative minimum tax on certain corporations. We express no opinion regarding other federal income tax consequences caused by the receipt or accrual of interest on or ownership of the Bonds.

5. The interest on the Bonds is exempt from personal income taxes imposed directly thereon by the State.

Very truly yours,

SUTIN, THAYER & BROWNE
A Professional Corporation

APPENDIX E

**FORM OF
CONTINUING DISCLOSURE UNDERTAKING**

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CONTINUING DISCLOSURE UNDERTAKING

This Continuing Disclosure Undertaking (the “Disclosure Undertaking”) is executed and delivered by the State Board of Finance (“Board”) of the State of New Mexico (the “State”) on behalf of the State in connection with the issuance by the State of \$37,040,000 Severance Tax Bonds, Refunding Series 2005B-1 (the “Series 2005B-1 Bonds”) and the \$21,095,000 Supplemental Severance Tax Bonds, Refunding Series 2005B-2 (the “Series 2005B-2 Bonds”, and collectively with the Series 2005B-1 Bonds the “Bonds”). The Bonds are being issued pursuant to a Bond Resolution adopted by the Board on May 24, 2005 (the “Resolution”).

BACKGROUND

1. The Bonds are being issued to advance refund certain outstanding maturities of the State of New Mexico Severance Tax Bonds, Refunding Series 2001A and Series 2002A and certain outstanding maturities of the State of New Mexico Supplemental Severance Tax Bonds, Series 2002A (collectively, the “Refunded Bonds”). The Refunded Bonds were issued for the purpose of financing the acquisition or construction of certain capital projects.

2. In order to allow the underwriters of the Bonds to comply with Rule 15c2-12 promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended (17 CFR Part 240, § 240.15c2-12) to the date hereof, the State is required to make certain continuing disclosure undertakings for the benefit of owners (including beneficial owners) of the Bonds.

3. This Disclosure Undertaking is intended to satisfy the requirements of said Rule 15c2-12, as in effect on the date hereof.

STATE COVENANTS AND AGREEMENTS

Section 1. Definitions.

(a) “Annual Financial Information” means the financial information or operating data with respect to the State, delivered at least annually pursuant to Section 2(a) and 2(b) hereof, of the type set forth in the sections of the final Official Statement identified on Exhibit A hereto. Annual Financial Information includes Audited Financial Statements.

(b) “Audited Financial Statements” means the annual financial statements for the State, prepared in accordance with generally accepted accounting principles, as in effect from time to time, audited by a firm of certified public accountants.

(c) “Event Information” means the information delivered pursuant to Section 2(d) hereof.

(d) “MSRB” means the Municipal Securities Rulemaking Board. The current address of the MSRB is 1900 Duke Street, Suite 600, Alexandria, Virginia, 22314, phone (703) 797-6600, fax (703) 797-6700.

(e) “National Repository” shall mean any Nationally Recognized Municipal Securities Information Repository for purposes of the Rule. Currently, the following are National Repositories:

Bloomberg Municipal Repository
100 Business Park Drive
Skillman, New Jersey 08558
Phone: (609) 279-3225
Fax: (609) 279-5962
Email: Munis@Bloomberg.com
Web: www.bloomberg.com/markets/rates/municontacts.html

DPC Data Inc.
One Executive Drive
Fort Lee, New Jersey 07024
Phone: (201) 346-0701
Fax: (201) 947-0107
Email: nrmsir@dpcdata.com
Web: www.dpcdata.com

FT Interactive Data
Attn: NRMSIR
100 William Street, 15th Floor
New York, New York 10038
Phone: (212) 771-6999; (800) 687-8466
Fax: (212) 771-7390
Email: NRMSIR@interactivedata.com
Web: www.ftid.com

Standard & Poor's Securities Evaluations, Inc.
55 Water Street
45th Floor
New York, New York 10041
Phone: (212) 438-4595
Fax: (212) 438-3975
Email: nrmsir_repository@sandp.com
Web: www.jjkenny.com/jjkenny/pser_descrip_data_rep.html

(f) "Official Statement" means the Official Statement dated May 24, 2005 delivered in connection with the original issue and sale of the Bonds.

(g) "Repository" means (i) each NRMSIR and (ii) any SID.

(h) "Rule" means Rule 15c2-12 promulgated by the SEC under the Securities Exchange Act of 1934, as amended (17 CFR Part 240, § 240.15c2-12), as the same may be amended.

(i) "SEC" means the Securities and Exchange Commission.

(j) "SID" means any State Information Depository operated or designated by the State that receives information from all issuers within the State. As of the date of this Disclosure Undertaking, no SID exists for the State.

Section 2. Provision of Annual Information and Reporting of Event Information.

(a) Commencing with the Fiscal Year ending June 30, 2005 and annually while the Bonds remain outstanding, the State agrees to provide or cause to be provided the Annual Financial Information to each Repository annually.

(b) Such Annual Financial Information shall be provided not later than 210 days after the end of each Fiscal Year for the State (i.e., each June 30). If the Audited Financial Statements are not available by the time the other Annual Financial Information must be provided, unaudited financial statements shall be provided as part of the Annual Financial Information. If not provided as a part of the Annual Financial Information, the Audited Financial Statements will be provided when available.

(c) The State may provide Annual Financial Information by specific reference to other documents, including information reports and official statements relating to other debt issues of the State, which have been submitted to each Repository; provided, however, that if the document so referenced is a final official statement within the meaning of the Rule, such final official statement must also be available from the MSRB.

(d) At any time the Bonds are outstanding, the State shall provide, in a timely manner, to the MSRB and any SID notice of any of the following events with respect to the Bonds, if material (provided, that any event under clauses (viii), (ix) or (xi) will always be deemed to be material):

- i. Principal and interest payment delinquencies;
- ii. Non-payment related defaults;
- iii. Unscheduled draws on debt service reserves reflecting financial difficulties;
- iv. Unscheduled draws on credit enhancements reflecting financial difficulties;
- v. Substitution of credit or liquidity providers, or their failure to perform;
- vi. Adverse tax opinions or events affecting the tax-exempt status of the security;
- vii. Modifications to rights of security holders;
- viii. Bond calls, other than mandatory sinking fund redemption;
- ix. Defeasances;
- x. Release, substitution or sale of any property securing repayment of the securities;
and
- xi. Rating changes.

(e) At any time the Bonds are outstanding, the State shall provide, in a timely manner, to the MSRB and any SID notice of any failure of the State to timely provide the Annual Financial Information as specified in Sections 2(a) and 2(b) hereof.

(f) Any filing under this Disclosure Undertaking may be made by transmitting such filing to the Texas Municipal Advisory Council (the "MAC") as provided at <http://www.disclosureusa.org>

unless the United States Securities and Exchange Commission has withdrawn the interpretive advice in its letter to the MAC dated September 7, 2004.

Section 3. Method of Transmission. Subject to technical and economic feasibility, the State shall employ such methods of electronic or physical information transmission as is requested or recommended by the Repositories or the MSRB unless otherwise required by law.

Section 4. Enforcement. The obligations of the State hereunder shall be for the benefit of the owners (including the beneficial owners) of the Bonds. The owner or beneficial owner of any Bonds is authorized to take action to seek specific performance by court order to compel the State to comply with its obligations under this Disclosure Undertaking, which action shall be the exclusive remedy available to it or any other owners or beneficial owners of the Bonds. Any such action shall be brought only in a State court of competent jurisdiction in Santa Fe County, New Mexico. Breach of the obligations of the State hereunder shall not constitute an event of default under the Resolution and none of the rights and remedies provided by the Resolution shall be available to the owners (including the beneficial owners) of the Bonds.

Section 5. Additional Information. Nothing in the Disclosure Undertaking shall be deemed to prevent the State from disseminating any other information, using the means of dissemination set forth in this Disclosure Undertaking or any other means of communication, or including any other annual information or notice of occurrence of an event which is not Event Information, in addition to that which is required by this Disclosure Undertaking; provided that the State shall not be required to do so. If the State chooses to include any annual information or notice of occurrence of an event in addition to that which is specifically required by this Disclosure Undertaking, the State shall have no obligation under this Disclosure Undertaking to update such information or include it in any future annual filing or Event Information filing.

Section 6. Term. This Disclosure Undertaking shall be in effect from and after the issuance and delivery of the Bonds and shall extend to the earliest of (i) the date all principal and interest on the Bonds shall have been paid or legally defeased pursuant to the terms of the Resolution; (ii) the date that the State shall no longer constitute an “obligated person” with respect to the Bonds within the meaning of the Rule; or (iii) the date on which those portions of the Rule which require this Disclosure Undertaking are determined to be invalid by a court of competent jurisdiction in a non-appealable action, have been repealed retroactively or otherwise do not apply to the Bonds.

Section 7. Amendments and Waivers. Notwithstanding any other provision of this Disclosure Undertaking, the State may amend this Disclosure Undertaking from time to time, and any provision of this Disclosure Undertaking may be waived, without the consent of the owners or beneficial owners of the Bonds upon the State’s receipt of an opinion of counsel experienced in federal securities laws to the effect that such amendment or waiver will not adversely affect compliance with the Rule. Any Annual Financial Information containing amended operating data or financial information will explain, in narrative form, the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided. If an amendment changes the accounting principles to be followed in preparing financial statements, the Annual Financial Information and Audited Financial Statements for the year in which the change is made will present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. The State shall provide notice of any such amendment or waiver to each Repository.

Section 8. Beneficiaries. This Disclosure Undertaking shall inure solely to the benefit of the State and the owners (including beneficial owners) from time to time of the Bonds, and shall create no rights in any other person or entity.

Section 9. Governing Law. This Disclosure Undertaking shall be governed by the laws of the State.

Date: _____, 2005

STATE BOARD OF FINANCE

By _____
President

By _____
Secretary

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EXHIBIT A

Portions Of The Official Statement
Containing The Type Of Information
To Be Included as Annual Financial Information

1. SEVERANCE TAX BONDING FUND AND DEBT SERVICE REQUIREMENTS
 - Investments
 - Issuance of Severance Tax Bonds
 - State Capital Program
 - Outstanding and Additional Severance Tax Bonds
 - Outstanding and Additional Supplemental Severance Tax Bonds
 - Table entitled “Severance Tax Bonding Fund Receipts, Disbursements and Transfers”
 - Table entitled “State of New Mexico Severance Tax Bonds - Projected Receipts, Debt Service Requirements and Coverage”
 - Fiscal Year and Scheduled Debt Service Columns
2. SEVERANCE TAX REVENUE
 - All
3. NATURAL GAS PRODUCTION AND SEVERANCE TAX REVENUE
 - Natural Gas Production
 - Data for chart entitled: “Natural Gas Subject to Taxation: Production, Revenues and Average Price”
 - Severance Taxes on Natural Gas
 - All
4. OIL PRODUCTION AND SEVERANCE TAX REVENUE
 - Oil Production
 - Data for chart entitled: “Oil Subject to Taxation: Production, Revenues and Average Price”
 - Severance Taxes on Oil
 - All
5. COAL PRODUCTION AND SEVERANCE TAX REVENUE
 - Severance Taxes on Coal
 - Data for chart entitled: “Coal Production, Pricing and Tax Rates”
 - Projections of Severance Tax Revenue from Coal
 - All
6. OTHER MINERAL PRODUCTION AND SEVERANCE TAXES
 - Any statements therein relating to the severance tax collected and tax rates
7. TAXATION OF ENERGY MINERALS NOT PLEDGED
 - All
8. APPENDIX A - GENERAL INFORMATION CONCERNING THE STATE OF NEW MEXICO
 - All
9. STATE OF NEW MEXICO FINANCIAL STATEMENTS (Audited)

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APPENDIX F

SPECIMEN BOND INSURANCE POLICY

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Financial Guaranty Insurance Policy

Ambac Assurance Corporation
One State Street Plaza, 15th Floor
New York, New York 10004
Telephone: (212) 668-0340

Obligor:

Policy Number:

Obligations:

Premium:

Ambac Assurance Corporation (Ambac), a Wisconsin stock insurance corporation, in consideration of the payment of the premium and subject to the terms of this Policy, hereby agrees to pay to The Bank of New York, as trustee, or its successor (the "Insurance Trustee"), for the benefit of the Holders, that portion of the principal of and interest on the above-described obligations (the "Obligations") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor.

Ambac will make such payments to the Insurance Trustee within one (1) business day following written notification to Ambac of Nonpayment. Upon a Holder's presentation and surrender to the Insurance Trustee of such unpaid Obligations or related coupons, uncanceled and in bearer form and free of any adverse claim, the Insurance Trustee will disburse to the Holder the amount of principal and interest which is then Due for Payment but is unpaid. Upon such disbursement, Ambac shall become the owner of the surrendered Obligations and/or coupons and shall be fully subrogated to all of the Holder's rights to payment thereon.

In cases where the Obligations are issued in registered form, the Insurance Trustee shall disburse principal to a Holder only upon presentation and surrender to the Insurance Trustee of the unpaid Obligation, uncanceled and free of any adverse claim, together with an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee duly executed by the Holder or such Holder's duly authorized representative, so as to permit ownership of such Obligation to be registered in the name of Ambac or its nominee. The Insurance Trustee shall disburse interest to a Holder of a registered Obligation only upon presentation to the Insurance Trustee of proof that the claimant is the person entitled to the payment of interest on the Obligation and delivery to the Insurance Trustee of an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee, duly executed by the Holder or such Holder's duly authorized representative, transferring to Ambac all rights under such Obligation to receive the interest in respect of which the insurance disbursement was made. Ambac shall be subrogated to all of the Holders' rights to payment on registered Obligations to the extent of any insurance disbursements so made.

In the event that a trustee or paying agent for the Obligations has notice that any payment of principal of or interest on an Obligation which has become Due for Payment and which is made to a Holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from the Holder pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such Holder will be entitled to payment from Ambac to the extent of such recovery if sufficient funds are not otherwise available.

As used herein, the term "Holder" means any person other than (i) the Obligor or (ii) any person whose obligations constitute the underlying security or source of payment for the Obligations who, at the time of Nonpayment, is the owner of an Obligation or of a coupon relating to an Obligation. As used herein, "Due for Payment", when referring to the principal of Obligations, is when the scheduled maturity date or mandatory redemption date for the application of a required sinking fund installment has been reached and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by application of required sinking fund installments), acceleration or other advancement of maturity; and, when referring to interest on the Obligations, is when the scheduled date for payment of interest has been reached. As used herein, "Nonpayment" means the failure of the Obligor to have provided sufficient funds to the trustee or paying agent for payment in full of all principal of and interest on the Obligations which are Due for Payment.

This Policy is noncancelable. The premium on this Policy is not refundable for any reason, including payment of the Obligations prior to maturity. This Policy does not insure against loss of any prepayment or other acceleration payment which at any time may become due in respect of any Obligation, other than at the sole option of Ambac, nor against any risk other than Nonpayment.

In witness whereof, Ambac has caused this Policy to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.

President



Secretary

Effective Date:

Authorized Representative

THE BANK OF NEW YORK acknowledges that it has agreed to perform the duties of Insurance Trustee under this Policy.

Form No.: 2B-0012 (1/01)

Authorized Officer of Insurance Trustee

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