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Tax Law

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INTRODUCTION

Cases decided during this Survey period[1] dealt with significant areas of tax law. The decisions affected the state of New Mexico's ability to tax transactions taking place on Indian lands within the state and to tax specific items of income. This article will focus on those New Mexico cases dealing with the state's power to tax transactions taking place in Indian Country,[2] the dividend income of nonresident corporations, and the income of nonresidents.[3] This article will also discuss two recent cases that considered the power of municipalities to structure excise taxes within the confines of a statute delegating such power.[4]

THE INDIAN CASES

As a general principle of tax law, an entity entitled to favored status (exemption from tax), is not ordinarily entitled to have its seller relieved of a sales or transaction tax on the basis that the seller usually passes the economic burden on to the buyer. A unique exception exists where Indian tribes bear the ultimate economic burden of a tax legally imposed on another person or entity. States do not have jurisdiction to tax Indians in Indian Country,[5] but may tax non-Indians doing business in Indian Coun-

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1. This article covers some of the cases decided during the last two Survey years, April 1980 through March 1982.

2. Ramah Navajo School Bd., v. Bureau of Revenue, ___ U.S. ___, 102 S. Ct. 3394 (1982).

3. F.W. Woolworth Co. v. Taxation and Revenue Dept., ___ U.S. ___, 102 S. Ct. 3128 (1982); Lung v. O'Cheskey, 94 N.M. 802, 617 P.2d 1317 (1980), *appeal dismissed*, 450 U.S. 961 (1981).

4. City of Albuquerque v. Cauwels & Davis, Management Co., 96 N.M. 494, 632 P.2d 729 (1981); City of Alamogordo v. Walker Motor Co., 94 N.M. 690, 616 P.2d 403 (1980).

5. 18 U.S.C. § 1151 (1976 & Supp. III 1979) defines Indian Country:

> Except as otherwise provided in sections 1154 and 1156 of this title, the term "Indian country," as used in this chapter, means (a) all land within the limits of any Indian reservation under the jurisdiction of the United States Government, notwithstanding the issuance of any patent, and, including rights-of-way running through the reservation, (b) all dependent Indian communities within the borders of the United States whether within the original or subsequently acquired territory thereof, and whether within or without the limits of a state, and (c) all Indian allotments, the Indian titles to which have not been extinguished, including rights-of-way running through the same. (June 25, 1948, ch. 645, 62 Stat. 757; May 24, 1949, ch. 139, § 25, 63 Stat. 94).

Outside of Indian Country, state taxes apply equally to Indians and non-Indians.

try. In certain situations, however, such an indirect tax on Indians may not be a permissible exercise of the state's taxing power.

Because of the special trust relationship between Indian tribes and the federal government, the imposition of state sales or transaction taxes on non-Indian sellers doing business with Indian governments in Indian Country may be an impermissible extension of the state's taxing power if: 1) the state tax imposed on the non-Indian seller invades an area of exclusive federal jurisdiction by interfering with the Indians' right to make their own laws and be ruled by them;[6] or 2) the state tax interferes with a federal statutory scheme evidencing a congressional intent to control the ultimate economic burden to be borne by a tribal government.[7] A state cannot legally impose on an Indian or a non-Indian a tax which has either of the above effects.[8]

The New Mexico Court of Appeals recently considered whether a New Mexico tax may be imposed on the gross receipts of a non-Indian contractor selling his services to Indians in Indian Country. The additional expense caused by the payment of the tax created an indirect economic burden on the tribe which paid the tax as passed on by the non-Indian seller.[9] The New Mexico court ruled that such a tax could be imposed. The United States Supreme Court disagreed.

The New Mexico Court of Appeals Decision

In *Ramah Navajo School Board, Inc. v. Bureau of Revenue,*[10] the New Mexico Court of Appeals held that the gross receipts of a non-Indian contractor building a school for the Ramah Navajo School Board[11] in Indian Country was subject to the New Mexico gross receipts tax. The court upheld the validity of the tax despite the tribe's showing that the school board would bear the "ultimate economic burden" of the tax. The court found no infringement on the tribal government of the Ramah

6. This doctrine is called the "infringement" test. *See infra* note 12.

7. This doctrine is called the "preemption" test. *See infra* note 15.

8. In White Mountain Apache Tribe v. Bracker, 448 U.S. 136 (1980), the United States Supreme Court recognized that the "infringement" and "preemption" tests are independent:

> The two barriers are independent because either, standing alone, can be a sufficient basis for holding state law inapplicable to activity undertaken on the reservation or by tribal members. They are related, however, in two important ways. The right of tribal self-government is ultimately dependent on and subject to the broad power of Congress. Even so, traditional notions of Indian self-government are so deeply ingrained in our jurisprudence that they have provided an important "backdrop," . . . against which vague or ambiguous federal enactments must always be measured.

Id. at 143.

9. Ramah Navajo School Bd. v. Bureau of Revenue, 95 N.M. 708, 710, 625 P.2d 1225, 1227 (Ct. App. 1980), *rev'd,* ___ U.S. ___, 102 S. Ct. 3394 (1982). *See* Hughes, *Indian Law, Survey of New Mexico Law: 1980–81,* 12 N.M.L. Rev. 409, 453–58 (1982).

10. 95 N.M. 708, 625 P.2d 1225 (Ct. App. 1980).

11. The Ramah Navajo School Board is a nonprofit corporation formed under New Mexico law and operated entirely by members of the Ramah Navajo Chapter. It is a "Tribal Organization" under 25 U.S.C. §450b(c) (1976).

Navajo Chapter of the Navajo Tribe. The court said that the tax did not infringe upon the tribe's right to "make their own laws and be governed by them,"[12] but failed to support that statement with any analysis.[13] The court of appeals noted that the tax was not on the tribe itself, but rather was legally imposed on the gross receipts of a non-Indian contractor who bore the legal liability for payment of the tax.[14] The court found no preemption, but inexplicably failed to conduct a meaningful inquiry into the various factors relevant to the preemption analysis.[15]

The New Mexico Court of Appeals apparently gave considerable weight to the fact that the "legal incidence"[16] of the tax rested with the non-Indian construction company. The court cited the Tenth Circuit decision

12. 95 N.M. at 710, 625 P.2d at 1227. This is a statement of the infringement test set forth in Williams v. Lee, 358 U.S. 217 (1959). In *Lee*, the United States Supreme Court held that states could not interfere with Indians' rights to make their own laws and be ruled by them. Such fundamental decisions were for the tribe and the federal government alone. Because the Indian Commerce Clause, U.S. Const. art. I, § 8, cl. 3, grants exclusive power to the federal government in matters relating to Indians, states are without the power to invade this area absent congressional approval. "Infringement" will be used throughout the text to denote a state action which interferes with tribal government in violation of the rule expressed in *Williams v. Lee*.

13. *See* 95 N.M. at 710, 625 P.2d at 1227.

14. *Id.*

15. In Warren Trading Post v. Arizona Tax Comm'n, 380 U.S. 685 (1965), the United States Supreme Court first decided that the application of a state "transactional privilege" on a non-Indian trading with Indians in Indian Country would interfere with the congressional intent to control the price of goods sold to Indians. Therefore, the Court held that the tax was statutorily preempted. The Court has expanded the reasoning of *Warren* to include broader and less explicit federal intentions expressed in various statutes. White Mountain Apache Tribe v. Bracker, 448 U.S. 136 (1980), and Central Machinery Co. v. Arizona Tax Comm'n, 448 U.S. 160 (1980). In these cases the "legal incidence" of the tax was on the non-Indian seller.

In *Ramah*, the New Mexico Court of Appeals cited its own decision in G.M. Shupe, Inc. v. Bureau of Revenue, 89 N.M. 265, 550 P.2d 277 (Ct. App.), *cert. denied*, 89 N.M. 321, 551 P.2d 1368 (1976), in support of its conclusion, yet apparently ignored a key aspect of *Shupe*. In *Shupe*, the court noted that no federal regulations existed indicating an intent "that the state not impose additional burdens" on the non-Indian conducting activities in Indian Country. *Id.* at 267, 550 P.2d at 279. Such was not the case in *Ramah*, and the court's reliance on *Shupe* was therefore misplaced.

16. The "legal incidence" of a tax is upon the person who is taxed; thus a tax imposed on sellers and indirectly passed on to buyers has its legal incidence on the sellers. In United States v. New Mexico, 581 F.2d 803 (10th Cir. 1978), *aff'd* ___ U.S. ___, 102 S. Ct. 1373 (1982), the Tenth Circuit held that the "legal incidence" was controlling when the state imposed a gross receipts tax on a contractor doing business with the United States. The court reasoned:

> Thus, the decisive issue in this case is whether the legal incidence of the challenged New Mexico taxes falls on the United States, regardless of where the economic burden ultimately rests.
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> . . . .
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> The Act specifically makes the gross receipts tax applicable to the doing of business in New Mexico without reference to whether that business is with the United States and, with uniformly applied exceptions, assesses the tax upon anyone receiving compensation. There is no evidence that the tax interferes with the performance of federal functions. The tax is not directly imposed on the United States and, although the contractors pass the tax onto the United States they are not required by the Act to do so.

581 F.2d at 806.

in *Mescalero Apache Tribe v. O'Cheskey,*[17] as authority for this proposition. In *Mescalero,* the plaintiffs did not demonstrate to the court's satisfaction that any federal statutes regulated the specific activity of building a resort in Indian Country. The court also found that any "economic burden" indirectly passed on to the tribe could be recovered by the tribe from the ultimate users of the resort. Therefore, the tribe did not bear the "ultimate economic burden" of the tax. Neither of the above situations was evident in the *Ramah* facts. The New Mexico court's apparent reliance on the legal incidence factor is particularly curious considering the fact that in *G.M. Shupe, Inc. v. Bureau of Revenue,*[18] the New Mexico Court of Appeals said that:

> the inquiry does not end with the recognition that the tax is on a non-Indian entity because the tax still has the potential for interference with protected rights. The two major issues are whether the subject of the tax is governed by substantial federal regulation and whether the imposition of the tax will infringe on Indian rights of self-government.[19]

The court's failure to conduct a particularized inquiry into the state, tribal, and federal interests implicated by the tax ignored a clear line of United States Supreme Court cases which command detailed inquiries into whether the tax is an infringement and whether an expressed or inferred congressional intent preempted the tax.[20] The New Mexico court should have noted that the allocation of the legal incidence is merely a threshold question. A tax whose legal incidence falls on an Indian cannot be enforced because the state is without jurisdiction to impose any tax directly on Indians in Indian Country.[21] If the legal incidence of a tax falls on a non-Indian doing business with Indians in Indian Country, the court must apply the infringement and preemption tests to determine whether the state tax is an infringement or whether the tax imposes a federally preempted economic burden on the tribe.[22]

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17. 625 F.2d 967 (10th Cir. 1980), *cert. denied,* 450 U.S. 959 (1981).

18. 89 N.M. 265, 550 P.2d 277 (Ct. App.), *cert. denied,* 89 N.M. 321, 551 P.2d 1368 (1976).

19. 89 N.M. at 267, 550 P.2d at 279.

20. In *Ramah Navajo School Bd. v. Bureau of Revenue,* the Supreme Court expressed disappointment with the New Mexico court's opinion: "Although we must admit our disappointment that the courts below apparently gave short shrift to this principle and to our precedents in this area [Indian self-determination], we cannot and do not presume that state courts will not follow both the letter and the spirit of our decisions in the future." ___ U.S. at ___, 102 S. Ct. at 3403. *See also* White Mountain Apache Tribe v. Bracker, 448 U.S. 136 (1980); Central Machinery Co. v. Arizona Tax Comm'n, 448 U.S. 160 (1980); Moe v. Confederated Salish & Kootenai Tribes, 425 U.S. 463 (1976).

21. McClanahan v. Arizona Tax Comm'n, 411 U.S. 164 (1973).

22. A tax whose legal incidence falls on a non-Indian doing business with Indians in Indian Country may be a proper exercise of the state's taxing power if the tax does not present an infringement question and is not preempted by federal statutes because the "ultimate economic burden" of the

The Supreme Court Decision

The United States Supreme Court reversed the New Mexico Court of Appeals and decided *Ramah* on the basis that certain relevant federal statutes preempted the state tax.[23] The Supreme Court discussed the notion that the allocation of the legal incidence of the tax is determinative of the preemption analysis, but squarely rejected the state's legal incidence argument.[24] The Supreme Court analyzed the *Ramah* facts and found that no infringement question was present. The Court did find, however, that activity related to building schools in Indian Country was the subject of a federal statutory scheme.

Because of the existence of these statutes, the Supreme Court determined that it should inquire into the congressional policy and intent surrounding the statutory scheme to determine if there was a preemption of New Mexico's taxation of school building activity in Indian Country.[25] The Court noted that the essential inquiry in preemption cases was to determine whether Congress intended to control the ultimate economic burden to be borne by Indians or the price to be paid for goods and services provided to Indians in Indian Country. The Court stated that congressional intent should be ascertained by analyzing specific federal

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tax can be passed on to a non-Indian. This is so even if the Indian has to wait until a project is completed to pass it on to the non-Indian. *See* Mescalero Apache Tribe v. O'Cheskey, 625 F.2d 967 (10th Cir. 1980), *cert. denied*, 450 U.S. 959 (1981). The legal incidence of a tax which is not an economic burden on a tribe, however, may create an infringement if the proper facts are shown. *See* Washington v. Confederated Tribes, 447 U.S. 134, 157 (1980). In *Washington*, the Supreme Court indicated that a tax with its legal incidence on a non-Indian may be impermissible if the mere existence and collection of the state's tax made it impossible for the tribe to collect a tax which it also imposed on a non-Indian. In such a case, the tribe would have to show that the double tax would cause businesses to leave the tribe's jurisdiction and would have to claim interference with its ability to make its own laws and be ruled by them. *See also* Central Machinery Co. v. Arizona Tax Comm'n, 448 U.S. 160, 164 n.3. *See also supra* note 15, wherein the cases cited, the tribes claimed that federal statutes preempted the state tax.

23. Ramah Navajo School Bd. v. Bureau of Revenue, ___ U.S. ___, 102 S. Ct. 3394 (1982).

24. The Supreme Court stated:

> The Bureau invites us to adopt the "legal incidence" test, under which the legal incidence and not the actual burden of the tax would control the pre-emption inquiry. Of course, in some contexts, the fact that the legal incidence of the tax falls on a non-Indian is significant. See *Washington v. Confederated Tribes*, 447 U.S. 134, 150–151, . . . (1980); *Moe v. Salish & Kootenai Tribes*, 425 U.S. 463, . . . (1976). However, in *White Mountain*, 448 U.S., at 151, . . . (1980), we found it significant that the economic burden of the asserted taxes would ultimately fall on the Tribe, even though the legal incidence of the tax was on the non-Indian logging company. Given the comprehensive federal regulatory scheme at issue here, we decline to allow the State to impose additional burdens on the significant federal interest in fostering Indian-run educational institutions, even if those burdens are imposed indirectly through a tax on a non-Indian contractor for work done on the reservation.

___ U.S. at ___, n. 8, 102 S. Ct. at 3402 n. 8.

25. *Id.* at ___, 102 S. Ct. at 3398–99.

statutes relating to the affected (burdened) activity.[26] The effect and allocation of the economic burden of the state tax and not the allocation of its legal incidence was the issue.[27]

The Supreme Court found that the power of Congress to regulate activities in Indian Country derives from the Indian Commerce Clause of the United States Constitution.[28] An exercise of congressional power pursuant to this clause will preempt state regulation in the same area even if the state had the power to regulate prior to the congressional action. Taxation of non-Indians doing business in Indian Country is a legitimate exercise of the state's taxing power so long as no tax is imposed directly on Indians. An inquiry into the intent of Congress to restrict such taxing power, however, is necessary whenever the economic burden of a state's tax is borne by Indians, even if the tax is imposed on a non-Indian. Such indirect taxation of Indians may be restricted by congressional enactments which, when viewed in light of the historical policy of Congress to further the economic development of tribes,[29] show a congressional intent to remove the state's authority to impose an economic burden by imposing an indirect tax on a tribe.

In applying this preemption analysis, the Supreme Court balanced the federal and tribal interests embodied in federal regulations concerning school construction activity in Indian Country, against the relevant state interests as follows: 1) Congress had legislated in the area of providing schools for Navajo children and had indirectly shown its concern that more money should be made available for the education of Indian children; 2) New Mexico's gross receipts tax constituted an additional "economic

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26. *Id.* at ___, 102 S. Ct. at 3399.

27. *See supra* note 24.

28. U.S. Const., art. I, § 8, cl. 3. The Court said:

> In *White Mountain*, we recognized that the federal and tribal interests arise from the broad power of Congress to regulate tribal affairs under the Indian Commerce Clause . . . and from the semi-autonomous status of Indian Tribes. . . . These interests tend to erect two "independent but related" barriers to the exercise of state authority over commercial activity on an Indian reservation: state authority may be pre-empted by federal law, or it may interfere with the Tribe's ability to exercise its sovereign functions.

___ U.S. at ___, 102 S. Ct. at 3398.

29. The Supreme Court noted:

> Pre-emption analysis in this area is not controlled by "mechanical or absolute conceptions of state or tribal sovereignty;" it requires a particularized examination of the relevant state, federal, and tribal interests. . . . The question whether federal law, which reflects the related federal and tribal interests, pre-empts the State's exercise of its regulatory authority is not controlled by standards of pre-emption developed in other areas. . . . Instead, the traditional notions of tribal sovereignty, and the recognition and encouragement of this sovereignty in congressional Acts promoting tribal independence and economic development, inform the pre-emption analysis that governs this inquiry.

Id. at ___, 102 S. Ct. at 3399 (citing White Mountain Apache Tribe v. Bracker, 448 U.S. 136 (1980)).

burden" on the tribe; 3) the additional "burden" placed on Ramah Navajo School Board interfered with congressional intent to make more money available for such activity; and 4) New Mexico did not identify any specific interest in imposing its tax, other than its general interest in raising tax revenue.[30] In light of the foregoing, the federal interest in tribal development outweighed the legitimate needs expressed by the state.[31] Therefore, the state's gross receipts tax could not be legally imposed on the non-Indian construction company building schools pursuant to federal enactments covering this activity. The imposition of the gross receipts tax was held to be an unjustified interference with the intent of Congress to make money available for the building of a school on Ramah Navajo land.

Future Considerations

In *Ramah,* the United States Supreme Court restated the limited significance of the legal incidence of a state tax imposed on non-Indians doing business in Indian Country. The legal incidence of a state tax is merely a threshold question which must show that the tax has its legal incidence on the non-Indian. If such a state tax is imposed on a non-Indian, a further inquiry into relevant federal and tribal interests as evidenced by congressional enactments is mandated. Whenever the power of Congress over a particular activity in Indian Country has been exercised by enactment of federal statutes, a state tax which creates an additional burden on the activity which is the subject of such legislation may be preempted. This is true even if the economic burden of the tax is only indirectly borne by an Indian tribe.

When a non-Indian sells goods in Indian Country, and taxes imposed on the non-Indian by the state create an indirect economic burden on a tribal government, the tax will be disallowed if Congress has legislated in the area and the court finds a congressional intent to control the ultimate economic burden to be borne by Indians or Indian tribes. Where, as in *Ramah,* a court finds only a generalized concern for the economic survival of the Indian tribe, the tax will be disallowed unless the state can show

30. *Id.* at ___, 102 S. Ct. at 3400–3403.

31. The Supreme Court stated that:

> Although there is no definitive formula for resolving the question of whether a State may exercise its authority over tribal members or reservation activities, we have recently identified the relevant federal, tribal, and state interests to be considered in determining whether a particular exercise of state authority violates federal law. *See White Mountain,* 448 U.S., at 141–145. . . .
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> . . . .
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> The State's interest in exercising its regulatory authority over the activity in question must be examined and given appropriate weight.

Id. at ___, 102 S. Ct. at 3398–99.

that its need to collect the tax outweighs the congressional intent to foster the tribe's economic development.

Such a case-by-case analysis leaves the state in an uncertain administrative position whenever it attempts to impose a tax on a non-Indian doing business in Indian Country. If Congress has legislated in an area which may be affected by the state's tax, the state will be unable to collect the tax from the non-Indian without a showing that a particular state interest in collecting the tax outweighs the federal and tribal interest underlying the legislation. This is true even if the federal interest is a general interest in the economic survival of the tribe which bears the ultimate indirect economic burden of the tax. Such a showing by the state is probably impossible whenever the tax receipts are going into general revenue funds of the state.

The irony of the balancing test proposed by the Supreme Court in *Ramah* lies in the inconsistency of the decision with the Court's earlier holding in *United States v. New Mexico*.[32] Had the federal government acted pursuant to its school building statute and contracted to build the *Ramah* school directly, without channeling funds through the tribe, a tax on the contractor would have been upheld on the basis that the contractor bore the legal incidence of the tax. The contractor escapes taxation, however, when the same funds are channeled through a tribal entity which shows that it bears the ultimate economic burden of the tax. Whether funds are channeled through a tribal entity or allocated to a contractor who contracts directly with the federal government, the responsibility for payment and the ultimate economic burden of the tax will be borne by the federal government, which provides the funds.

JURISDICTION TO TAX INTERSTATE CORPORATE INCOME

In *F.W. Woolworth Co. v. Taxation and Revenue Department*,[33] the United States Supreme Court reversed the New Mexico Supreme Court.[34] The Supreme Court held that New Mexico could not include Woolworth's

32. ___ U.S. ___, 102 S. Ct. 1373 (1982). In *United States v. New Mexico*, the Supreme Court considered whether three contractors, contracting directly with the United States under "advance funding" procedures, could be required to pay the New Mexico gross receipts tax on amounts distributed directly to suppliers from a United States treasury funded account. The contractors acknowledged the validity of and paid the tax on the fees they received which were not issued directly from the treasury funded account. The Supreme Court held that New Mexico could impose its tax on the disputed amounts, and that the doctrine of federal immunity from state taxation did not bar the state from imposing its tax where the state tax was legally imposed on the contractor and not directly on the United States. The Court, citing Alabama v. King & Boozer, 314 U.S. 1, 9 (1941), stated: "Thus, immunity may not be conferred simply because the tax has an effect on the United States, or even because the Federal Government shoulders the entire economic burden of the levy." ___ U.S. at ___, 102 S. Ct. at 1382.

33. ___ U.S. ___, 102 S. Ct. 3128 (1982).

34. Taxation and Revenue Dep't v. F.W. Woolworth Co., 95 N.M. 519, 624 P.2d 28 (1981).

foreign subsidiary dividend income as taxable income. The Court stated that the tax failed to meet due process standards because it did not bear a rational relationship to benefits or protection conferred by New Mexico.[35] The Court also held that New Mexico could not force Woolworth to pay additional state tax because of certain "gross-up"[36] amounts which Woolworth was required to include in its federal tax return by reason of a foreign tax credit.

In *Woolworth,* New Mexico had attempted to tax the apportioned share of dividends received by Woolworth from its investments in its foreign subsidiaries. The validity of the tax on these amounts depended upon the New Mexico Supreme Court's interpretation of the "unitary-business principle."[37] Under this principle, the dividends and contributions of a subsidiary company to its parent must result from the operation of a business by the parent and its subsidiaries as a single entity, and not from the operation of the dividend-producing entities as independent businesses. The United States Supreme Court found that New Mexico misconstrued the unitary-business principle. In order for a unitary-business to exist, the court must find the "underlying economic realities of a unitary business."[38] Unless the activities of an interstate corporation are functionally related to those of its subsidiaries, the state does not have jurisdiction to tax the dividend income from the subsidiaries of an interstate corporation. New Mexico never demonstrated the existence of any of the features which create an integrated business. Instead the state based its claim for taxes on the fact that the potential for functional integration and operation of the business as a whole existed.

The United States Supreme Court analyzed the facts of the case and determined that the parent company treated each dividend-producing subsidiary as a separate entity and that each subsidiary operated as a separate business. Therefore, the independent entities were not operated in a manner which allowed state taxation based upon dividends paid by the subsidiary to the parent. The Court cited its decision in the companion case

35. ___ U.S. at ___, 102 S. Ct. at 3139.

36. The New Mexico Supreme Court defined "gross-up" as follows:

> The literal meaning of the term "gross-up" has been lost in the labyrinth. However, it is used here to refer to the option an American multinational corporation has under the federal income tax law to claim credit for income taxes paid to foreign governments by its foreign subsidiaries. I.R.C. §§ 901–908. It results in a federal tax benefit to the corporation based on an adjustment made to federal taxable income.

95 N.M. at 521, 624 P.2d at 30.

37. The United States Supreme Court stated that "[t]he 'linchpin of apportionability' for state income taxation of an interstate enterprise is the 'unitary-business principle.'" ___ U.S. at ___, 102 S. Ct. at 3134.

38. Exxon Corp. v. Wisconsin Dep't of Revenue, 447 U.S. 207, 223-24 (1980) (quoting Mobil Oil Corp. v. Comm'r of Taxes, 445 U.S. 425, 441 (1980)).

of *ASARCO Inc. v. Idaho Tax Commission*,[39] for the proposition that "the *potential* to operate a company as part of a unitary business is not dispositive when, looking at 'the "underlying economic realities of a unitary business,"' the dividend income from the subsidiardies [sic] *in fact* is 'derive[d] from "unrelated business activity" which constitutes a "discrete business enterprise."'"[40]

The United States Supreme Court also disallowed New Mexico's attempt to tax gross-up amounts. The Supreme Court reasoned that gross-up amounts are tax items which the federal government "deems" Woolworth to have received and are not an accurate reflection of income. Therefore, such amounts were not a proper subject of the state's corporate income tax. Further, because this item of gross-up income arose from Woolworth's foreign subsidiaries which were subject to taxation by foreign nations, there was an insufficient nexus with the State of New Mexico to allow the state to impose its tax on these amounts.[41]

JURISDICTION TO TAX OUT-OF-STATE RESIDENTS

In *Lung v. O'Chesky*,[42] the New Mexico Supreme Court held that New Mexico could tax the income of nonresidents who worked on federal enclaves located in New Mexico. In *Lung*, the plaintiffs sought relief from New Mexico taxes on three grounds. First, the plaintiffs contended that an insufficient "fiscal relation" existed between them and New Mexico because the affected taxpayers did not get enough benefit from their tax dollars.[43] Second, the plaintiffs contended that the New Mexico apportionment procedure for deductions and exemptions discriminated against nonresidents.[44] Third, the plaintiffs argued that New Mexico did not have jurisdiction to tax income earned in a federal enclave.[45] In the alternative, the plaintiffs argued that if New Mexico was allowed to tax their incomes, it could not deny them grocery and medical rebates offered to state residents[46] solely on the basis of their status as nonresidents.

The New Mexico Supreme Court responded to the plaintiffs' argument in a brief but well-reasoned opinion. The court stated that first, the power to tax does not rest on a measurable economic duty of a state to its

39. ___ U.S. ___, 102 S. Ct. 3103 (1982).

40. ___ U.S. at ___, 102 S. Ct. at 3134 (quoting *Exxon*, 447 U.S. at 223–24, and *Mobil Oil*, 445 U.S. at 441, 442, 439) (emphasis by the Court).

41. ___ U.S. at ___, 102 S. Ct. at 3139.

42. 94 N.M. 802, 617 P.2d 1317 (1980), *appeal dismissed*, 450 U.S. 961 (1981). The Supreme Court dismissed the appeal for lack of a substantial federal question.

43. 94 N.M. at 804, 617 P.2d at 1319.

44. *Id.*

45. *Id.*

46. *Id.* at 805, 617 P.2d at 1320.

citizens, but on less tangible benefits.[47] The court held that a benefit sufficient to support an income tax was the opportunity to exercise "intelligence, skill and labor while employed in the State of New Mexico."[48] Second, the Supreme Court held that because the state may tax income of nonresidents earned in the state and may not tax income of nonresidents not earned in the state, it followed that deductions and exemptions should be apportioned in the same way as taxable income.[49] Third, as to jurisdiction to tax income earned in a federal enclave, the court cited the "Buck Act"[50] which states that "no person shall be relieved from liability for any income tax levied by any State, . . . by reason of his residing within a Federal area."[51]

After finding the New Mexico tax and procedure constitutional and applicable to the plaintiffs, the New Mexico Supreme Court upheld the denial of credits to nonresidents. The court found that a rational basis existed for the legislature to believe that nonresidents did not actually pay gross receipts tax on grocery and medical services in New Mexico. Therefore, the plaintiffs were not entitled to credits whose purpose was to rebate these amounts.[52] This opinion is in line with the clear weight of authority and, if decided differently, could have resulted in significant restrictions on the state's ability to tax the income of nonresidents.

AUTHORITY TO IMPOSE MUNICIPAL TAXES

During the Survey period, the New Mexico courts had two opportunities to consider municipal taxation pursuant to authority granted by the state legislature. In *City of Albuquerque v. Cauwels & Davis, Management Co.*,[53] the City of Albuquerque imposed an occupation tax. Because the classification of businesses was not in strict accord with the granting statute,[54] the city could not legally impose the tax. In disallowing the tax,

47. *Id.* at 804, 617 P.2d at 1319.
48. *Id.*
49. *Id.*
50. 4 U.S.C. §§ 106–110 (1976).
51. *Id.*
52. 94 N.M. at 805, 617 P.2d at 1320.
53. 96 N.M. 494, 632 P.2d 729 (1981).
54. N.M. Stat. Ann. § 3-38-3 (1978), provides in part:

> A. A municipality may impose an occupation tax and classify any occupation, profession, trade, pursuit, corporation and other institution and establishment, utility and business of whatever name or character, like or unlike, and not licensed as authorized in Section 3-38-1 NMSA 1978, or not licensed by the municipality as authorized by any other law.
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> B. . . . A municipality may classify occupations and impose an occupation tax on each occupation. If a municipality chooses to classify for the purpose of levying an occupation tax, the classifications which shall be used are:
>
> (1) manufacturing;
>
> (2) utility;

the New Mexico Supreme Court stated that the rules of construction to be applied to such a statute were: 1) "the grant of power to the municipality must be strictly construed, and the municipality must keep closely within its limits"[55] and 2) "a municipality is without power to change, by local law, the method of collecting taxes established by the legislature."[56] The court stated that the policy underlying these strict rules of construction was that "when taxing authority is delegated . . . taxpayers should not be subjected to the burden of taxation without clear warrant of law."[57] The court then held the municipal ordinance to be without force and effect.

In *City of Alamogordo v. Walker Motor Co.*,[58] the New Mexico Supreme Court considered whether a municipal occupation tax passed by the City of Alamogordo and authorized by N.M. Stat. Ann. § 3-38-3 (1978), was a proper exercise of delegated municipal taxing authority.[59] In *Alamogordo*, the city had imposed an occupation tax, measured by the amount of business receipts, on sales of motor vehicles.[60] The plaintiff challenged the tax because the applicable statute[61] provides that no municipality may impose an excise tax on any incident relating to motor vehicles. The city argued that the New Mexico statutes were in conflict on this issue.[62] After finding the tax to be an "excise tax,"[63] the court resolved the apparent contradiction in the New Mexico statutes in favor of the plaintiff. The court found that the proper rule of construction in such a case was "where one statute deals with a subject in general terms and another deals with a part of the same subject in a more specific way, the more specific statute will be considered to be an exception to the general statute."[64] The court also held that "where the conflict between an earlier act and a later act is clear and irreconcilable, the later act, as the most recent expression of legislative intent, will be considered to have repealed by implication the

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(3) wholesale;
(4) retail;
(5) banking; and
(6) financial.

This section was repealed in 1981 by 1981 N.M. Laws, ch. 37, § 3, and replaced by N.M. Stat. Ann. § 3-38-3 (Cum. Supp. 1982), relating to authorization for business registration fees.

55. 96 N.M. at 496, 632 P.2d at 731.
56. *Id.*
57. *Id.*
58. 94 N.M. 690, 616 P.2d 403 (1980).
59. *Id.* at 691, 616 P.2d at 404.
60. *Id.*
61. N.M. Stat. Ann. § 3-18-2(C)(3)(d), and (D) (Cum. Supp. 1982).
62. 94 N.M. at 692, 616 P.2d at 405.
63. *Id.*
64. *Id.* (citing New Mexico Bureau of Revenue v. Western Elec. Co., 89 N.M. 468, 553 P.2d 1275 (1976)).

earlier conflicting statute to the extent of the inconsistency."[65] The court applied the above rules of construction and held that the local tax was invalid.

These cases, although not of great importance, provide some guidance for resolving future issues regarding the taxing jurisdiction of municipal governments, and provide guidance for the drafters of future municipal taxing ordinances. Further, these cases suggest that municipalities should read carefully the statutes granting them specific taxing powers and should fashion their municipal tax statutes according to the specific terms of the enabling statute.

CONCLUSION

The State of New Mexico won some cases and lost some cases during the Survey period, but in doing so it has been able to test the validity of its taxes in the United States Supreme Court, and obtain guidance as to that Court's action in future cases. It is hoped that these cases will lead to a better understanding of the state's right to tax, and the constitutional limits placed on the exercise of this sovereign right by virtue of the due process clause and the doctrine of federal supremacy.

65. 94 N.M. at 692, 616 P.2d at 405.