Opinion No. 50-5316

August 11, 1950

BY: JOE L. MARTINEZ, Attorney General

TO: State Land Office Santa Fe, New Mexico. Attention: George Graham

*{*172}* I am writing in reply to your letter of August 8, 1950 regarding the recent ruling of the Department of Internal Revenue, under the provisions of which the Department of Internal Revenue is making a demand for the payment of documentary stamp tax on all sales and leases of state land.

The pertinent ruling of the Department of Internal Revenue Code provides as follows:

"M.T. 39 (Internal Revenue Bulletin. 1950-9,9) holds that conveyance of real property to or by a State or political subdivision or corporate instrumentality thereof are not exempt from documentary stamp tax merely by reason of the governmental character of one of the parties to the transaction. That ruling revoked S.T. 897 (C.B. 1940-1, 256), in which it was held that a conveyance of realty to a local housing authority, which is an instrumentality of either a State or a political subdivision thereof, is not subject to stamp tax. Because of the long-standing position of the Bureau and the consequent reliance on this ruling in transactions involving *{*173}* conveyance of real property, it is held that, under the authority contained in section 3791(b) of the Internal Revenue Code, the ruling published as M.T. 39, supra, will not be applied retroactively, except that any tax which has been paid on conveyances of real property falling within the scope of that ruling will not be refunded.

Accordingly, subject to the limitations stated above with respect to refunds, conveyances of real property prior to May 1, 1950, made to or by a State or a political subdivision or corporate instrumentality thereof will not be subject to the documentary stamp tax imposed by section 3482 of the Code, as amended. However, such conveyances made on and after May 1, 1950, will not be exempt from the tax imposed by that section merely by reason of the governmental character of one of the parties to the transaction."

There is a certain amount of ambiguity in the regulation and it is wrong either because it is too comprehensive in its language or the attempt to apply the ruling to sale and lease of state land by this office is erroneous.

Under the provisions of the Enabling Act, approved by Congress on June 20, 1910, 36 Stats. 557, it was provided in Section 10 that the grant of public lands was to be held in trust by the state and certain specific limitations were incorporated in the regulation as to the sale, transfer, use, and purpose for which the income derived from these lands were to be used. The income to be derived from the state lands was to be used

primarily to support the educational systems of the state. This income forms the backbone for our public educational system.

The Constitution of the State of New Mexico was adopted on January 21, 1911 and the Constitution in Article 21 specifically incorporated the Enabling Act as an inherent part of the legislation. On August 21, 1911, 37 Stats. 39, Congress by congressional resolution affirmed the admission of New Mexico into the Union on an equal footing with the rest of the states and the admission of the state was concluded by proclamation of the President on January 6, 1912. 37 Stats. 1723.

It is obvious from the foregoing that the function of the Land Office in transfering state lands by lease, contract, or any other manner is the performance of an integral and substantial part of the state government. Furthermore, the dedication of these lands and the income derived from them to the maintenance of the educational system of the State of New Mexico are standards imposed by Congress itself.

There is no desire to trace the long history of the principle that state governments are immune from federal taxes. The principal of reciprocal immunity by the United States and the several states goes back to the decision in McCulloh vs. Maryland, 4 Wheat. 316 which held that a bank, chartered by the United States was immune from a stamp tax imposed on the banks circulating currency. The reciprocal principle was determined in Collector vs. Day (Buffington vs. Day) 11 Wall. U.S. 113, which held that a state judge was immune from a federal income tax.

There has been a gradual erosion from the general principle with the passage of time and the change in functions of state government. In the first group may be said to fall those cases in which the immunity of the state is absolute from federal taxation. In such cases the tax is attempted to be levied on a purely governmental *{*174}* function. In the second group, where there is no immunity, the state government is engaging in a proprietary function such as is carried on by private individuals. In this type of cases is the sale of spring water, the sale of intoxicating liquors, taxes on the conducting of athletic contests.

The Supreme Court has held that the sale of its natural resources by the state, being essentially a governmental function, the federal government cannot tax the proceeds thereof. The fact that profits are derived from such sale is not important. See Brush vs. Commissioner of Internal Revenue, 300 U.S. 352; Mayo vs. United States, 319 U.S. 441; Burnet vs. Coronado Oil and Gas Company, 285 U.S. 393.

In the case of U.S. vs. N.Y., 140 F.2d 608, a federal tax of two cents per gallon on bottled water was imposed on the state of New York which, through a commission, was engaged in the bottling and selling of such mineral water. In his opinion Judge Chase stated that there were five different theories of immunity which had been urged: (1) activities must be of a "strictly governmental character"; (2) immunity exists only when "essential governmental functions" are involved; (3); the activities must involve the "usual governmental functions"; (4) the activities must be traditionally governmental; (5)

no immunity exists where "the activity corresponded in all essentials to a business usually carried on by private enterprise." This case was affirmed in 326 U.S. 572. It might be pointed out that Justice Frankfurter in his opinion takes somewhat more comprehensive view of the taxability of the state by the federal government, but it is doubtful whether the broadness of his language can be interpreted to justify the imposition of the tax on such essential governmental functions as are found in this case.

It is, therefore, my opinion that the state is not liable to pay the documentary tax stamp on the sale, lease, or other transfer of state lands.

I am sending a copy of this opinion to the Collector of Internal Revenue at Albuquerque and to the United States District Attorney for this district.