Opinion No. 63-145

October 30, 1963

BY: OPINION of EARL E. HARTLEY, Attorney General

TO: Mr. Charles C. Brunacini Commissioner of Revenue Bureau of Revenue Santa Fe, New Mexico

QUESTION

QUESTIONS

1. Are the gross receipts derived from sales of tangible personal property to the United States government, the State of New Mexico, or one of the other entities exempted under Section 72-16-5, N.M.S.A., 1953 Compilation, exempt from all of the taxes levied by the Emergency School Tax Act?

2. Are the gross receipts derived from sales of tangible personal property sold in interstate commerce exempt from all of the taxes levied by the Emergency School Tax Act?

CONCLUSIONS

1. No.

2. No.

OPINION

*{*327}* **ANALYSIS**

The Emergency School Tax Act, Sections 72-16-2, et seq., N.M.S.A., 1953 Compilation, places a number of different business activities in different classifications, and taxes them separately. Prior to the final retail sale of any given item of tangible personal property, that same property may have been involved in a number of other taxable transactions. The preparation of the property for final sale may have involved extraction of natural resources, taxable under Section 72-16-4.2, or processing of natural resources, taxable under Section 72-16-4.3 (b), or manufacturing, exempt under Section 72-16-4.3 (c), or wholesaling, exempt under Section 72-16-4.4 except as to alcoholic beverages. The sale may have been handled by an agent, whose commission is taxable under Section 72-16-4.12. The retail business itself is taxed under Section 72-16-4.5, unless the goods sold are extracted, processed, or manufactured by the person selling them at retail, in which case the retail sale is taxed under Section 72-16-12 at the same rate as a retail business classified under Section 72-16-4.5.

When the final retail sale is to one of the exempt entities specified in Section 72-16-5, or is in interstate commerce, the question is whether the gross receipts derived from that sale are exempt from all of the taxes imposed by the Emergency School Tax Act, or do they remain subject to some of the taxes, particularly those taxes imposed on a business privilege exercised and completed prior to the final sale. As an example of the problem posed, suppose a uranium company operates a mill in New Mexico, and processes uranium ore in that mill to produce uranium concentrate. This is taxable as processing under Section 72-16-4.3 (b). The uranium company then sells the uranium concentrate to the United States, and, moreover, the sale is in interstate commerce. When a processor of natural resource products sells them at retail, his gross receipts are taxable under Section 72-16-12, which tax is in addition to the tax imposed by Section 72-16-4.3 (b). Since the sale is to the United States, and is in interstate commerce, however, we must consider the effect *{*328}* of our exemption provisions, and must also consider the scope of the power of a state to reach such transactions with its tax laws.

In answering the questions posed, we propose to discuss first what our statutes purport to do, second what the state has power to do, and last the effect of two interesting and conflicting New Mexico cases on the subject.

Section 72-16-5, N.M.S.A., 1953 Compilation provides:

"None of the taxes levied by the Emergency School Tax Act, as amended, shall be construed to apply to:

A. Sales of tangible personal property, other than metalliferous mineral ores, whether refined or unrefined, made to the government of the United States, its departments or agencies;

B. sales of tangible personal property, other than metalliferous mineral ores, whether refined or unrefined, made to the state of New Mexico or any of its political subdivisions; and

C. sales of tangible personal property, other than metalliferous mineral ores, whether refined or unrefined, made to nonprofit hospitals, religious or charitable organizations in the conduct of their regular hospital, religious, or charitable functions."

This statute is somewhat of an anomaly. Whereas the school tax act imposes taxes on the person engaged in business, and concerns itself with the nature of the seller's business, this statute looks beyond that to the status of the purchaser, and provides for an exemption which actually applies to the seller, since the purchaser is not liable for any tax, as such, and pays none. However, it is this section that gives rise to questions of the taxability of the gross receipts of a business derived from transactions with the United States, or other exempt entities. It will be noticed that the exemption applies only to the sale of tangible personal property, and not to the sale of services.

Section 72-16-8, N.M.S.A., 1953 Compilation, provides:

"In the case of businesses classified under sections 2, 3, 10, and 12 of this 1959 act, the rate shall be applied to the entire business of the taxpayer, regardless of the fact that deliveries may be made outside the state. . ."

The specific references in this statute are to persons engaged in the businesses of extracting, processing, selling services (other than professional) on a price or fee basis, and acting as factors, agents, or brokers on a commission basis. Clearly, this section purports to tax such businesses, regardless of whether the ultimate product of the business is delivered in interstate commerce. This would apply to one who extracts mineral resources in this state and sells the extracted minerals in interstate commerce, one who processes or refines mineral resources in this state and then sells the processed product in interstate commerce, one who provides a service in this state, such as laundering clothes, but then delivers the property on which the service was performed into another state, and one who sells property on a commission basis in New Mexico, but delivers the property sold in another state, or causes it to be delivered in another state.

*{*329}* Section 72-16-9, N.M.S.A., 1953 Compilation, provides:

"If any person engaged in any business subject to tax under this act shall ship, transmit or transport his products, or any part thereof, out of the state without making sale of such products, or shall ship his products outside of the state in an unfinished condition, or make a sale of the same which is exempt from tax under the provisions of this act, the value of the products or articles in the condition or form in which they existed when transmitted or transported out of the state and before they enter interstate commerce or before such exempt sale shall be the basis for the assessment of the tax on such business, and the tax commission (bureau of revenue) shall prescribe equitable and uniform rules for ascertaining such value."

At first glance, this section would seem to say that our tax will be imposed on sales in interstate commerce, except that the tax not be imposed on the sales price, but on a computed value prior to sale. It also seems to impose the tax on a sale to an exempt entity. If so, one wonders why any exemptions were granted in the first place. But we feel that we must give effect to every section of the statutes, and where a specific exemption has been granted, such as the exemption for sales to the United States, that exemption must be given effect notwithstanding the provisions of Section 72-16-9. We must also give effect to the immunity of interstate commerce from direct taxation by a state. In this respect, we note that the first sentence of Section 72-16-9 shows that that section is only applicable to a business "subject to tax under this act." It remains to be seen whether, and to what extent, businesses engaging in interstate commerce are subject to the act.

Sections 72-16-4.2 (C) and 72-16-4.3 (D) both state that the measure of the tax imposed by those sections shall be the value of the entire production in this state,

regardless of the place of sale or the fact that delivery may be made to a point outside the state. These provisions say no more than has already been said by the general wording of Section 72-16-8, which has been quoted above.

Lastly, we must consider the provisions of Section 72-16-12, N.M.S.A., 1953 Compilation. To avoid tiresome quotation, that section provides that businesses classified as extractors, processors, manufacturers, and wholesalers shall pay an additional tax equal to the tax imposed on retailers if those businesses engage in selling their products or goods at retail **in this state.** Clearly, this additional tax would not apply to the named businesses if they sold their products or goods in another state or in interstate commerce. In our opinion, this provision was inserted to keep local businesses competitive in foreign retail markets. If they had to pay a local retail tax on a sale in interstate commerce, they might be priced out of the market in another state. Moreover, where the sale actually takes place in another state, that sale is subject to tax in that state, and the total transaction would be subjected to double taxation, thus discriminating against interstate commerce.

The foregoing, then, is the statutory framework of our school tax act. In general, it may be said that it attempts to reach every business that the state has power to tax, specifically exempting only sales to certain named entities, and retail sales in interstate commerce made by extractors, processors, manufacturers, and *{*330}* wholesalers. Now let us turn to the question of the power of the state to tax sales to the United States, and sales in interstate commerce, without regard to any exemptions.

A state may not tax a sale in interstate commerce, nor gross receipts derived therefrom, nor can it levy a privilege tax against the privilege of engaging in interstate commerce. **Albuquerque Broadcasting Co. v. Bureau of Revenue,** 51 N.M. 332, 184 P.2d 416. A state can tax an essentially local activity that is only indirectly connected with interstate commerce, as, for example, the receipts of a locally published magazine arising from advertising contracts, even though the magazines are later sold and distributed in interstate commerce. **Western Live Stock v. Bureau of Revenue,** 41 N.M. 141, 65 P.2d 863, **affirmed,** 303 U.S. 250, 82 L. Ed. 823, 58 S. Ct. 546. These cases control the outcome where the tax is on the retail transaction (sales tax) or where the tax is on the privilege of engaging in the retail transaction (privilege tax) measured by the gross receipts from interstate commerce. Therefore, without regard to the possible interpretations that might be given our statutes, our school tax does not apply to a transaction in interstate commerce. But the question to be answered now is whether such businesses as extracting and processing minerals are transactions in interstate commerce, even though the products so extracted or processed are ultimately sold in interstate commerce.

In the case of **Black Hawk Consolidated Mines Co. v. Gallegos,** 52, N.M. 74, 191 P.2d 996, the mining company was engaged in the business of extracting gold and was also in the business of selling gold. The sales were in interstate commerce. Our Supreme Court held that the extraction tax applied to the gross receipts derived from that sale, even though the sale was in interstate commerce. The rationale was that the

business of mining was a purely local activity, complete before any interstate sale or shipment. The imposition of our tax on that activity did not burden interstate commerce. Looking further, we find that the Supreme Court of the United States agrees with our Supreme Court. In the case of **American Manufacturing Co. v. City of St. Louis,** 250 U.S. 459, 39 S. Ct. 522, 63 L. Ed. 1084, the city of St. Louis imposed a privilege tax on manufacturers, measured by their gross receipts from sales of the manufactured products. The manufacturing company sold its manufactured products in interstate commerce. The Supreme Court of the United States upheld the tax, reciting substantially the same arguments that were set out in the **Black Hawk** case, supra. The Court went on to point out that the city could have made the tax due and payable just as soon as the manufacturing was completed, without waiting for a sale of the manufactured products. Instead, the city delayed the payment date of the taxes to such time as the manufactured products were sold, allowing the manufacturer to obtain money with which to pay the taxes. The Court agreed that it was reasonable to measure the value of the privilege of manufacturing by gross receipts from sales, even sales in interstate commerce.

These decisions control the question of the exemption to be accorded to sales in interstate commerce. It is only the transaction in interstate commerce itself that is exempt from our tax, the ultimate transaction. Our taxes on transactions performed prior to the sale in interstate commerce still apply to the gross receipts derived from the sale. These include our taxes on extractors, processors, business services, commission agents, custom refining and perhaps others. It is easier to state what is exempt; *{*331}* only the privilege of engaging in the transaction in interstate commerce is exempt.

This leaves only the question of the scope of the exemption for sale to the United States and the other exempt entities specified in Section 72-16-5. That section provides that **none** of the taxes levied by the emergency school tax shall apply to such sales.

The State of Mississippi has a tax identical to ours in legal effect, and it also has an exemption provision allowing the taxpayer to deduct his gross receipts derived from sales to the United States before computing any tax due under the Mississippi tax statute. Mississippi, just like New Mexico, imposes separate taxes on the business of preparing lumber for sale and on the business of selling that lumber. The case of **Stone v. Green Lumber Co.,** 191 Miss. 414, 1 So.2d 764, involved a lumber company that both manufactured lumber and sold it. The lumber company contended that, on its sales of lumber to the United States, it was entitled to deduct those gross receipts in computing the manufacturing tax as well as the retail tax. The Mississippi court rejected this argument, and held that the exemption only extended to the tax imposed on retailing, not the tax imposed on manufacturing. It pointed out that the manufacturing was a purely local activity that was completely performed prior to any sale, and was not therefore a tax on the sale. The privilege of manufacturing was performed solely within the state of Mississippi, and could not be subjected to taxation in another state. The effect of imposing the tax was simply to increase the overhead of the business, and the price of the products, but it was in no sense a tax on the United States, nor on a transaction to which the United States was a party.

A **sales** tax, the legal incidence of which falls on the purchaser, cannot be imposed on a sale of property to the United States, **Kern-Limerick v. Scurlock,** 347 U.S. 110, whereas a privilege tax imposed equally on all engaged in the same business may be imposed on a retailer even where he makes a retail sale to the United States, **United States and Olin Mathieson Chemical Corp. v. Department of Revenue,** 202 F. Supp. **757, affirmed,** 371 U.S. 21, 9 L Ed. 2d 95, 83 S. Ct. 117. The New Mexico emergency school tax is a privilege tax imposed on certain businesses for the privilege of engaging in them, and measured by the gross receipts derived from engaging in them. **Bradbury & Stamm Construction Co. v. Bureau of Revenue,** 70 N.M. 226, 372, P.2d 808. These authorities establish the **power** of the state to impose a privilege tax on businesses dealing with the United States, its departments and agencies. (There is no question of the power of the state to impose the same tax on businesses dealing with the state, or with the other exempt entities enumerated in Section 72-16-5.) However, as noted before, we have a statute exempting sales to the United States, its departments and agencies. Let us now turn to two New Mexico cases construing the scope of the exemption.

The first is **Gallup American Coal Co. v. Beall,** 39 N.M. 188, 43 P.2d 927 (1935). When this case was decided, the emergency school tax act was less than one year old. The coal company was engaged in the business of extracting coal, and was also engaged in the business of selling that coal at retail; each of these activities was subject to a separate tax, just as each is today. Some of the sales of coal were made to the United States, and the coal company contended that the gross receipts of those sales were exempt from **any** of the taxes imposed by the statute. The state contended that the *{*332}* exemption extended only to the tax on the privilege of retailing, but not to the tax on the privilege of extracting, which was an entirely separate and complete business. The exemption provision in effect at that time provided, in pertinent part as follows:

"None of the taxes levied by this act shall be construed to apply to . . . sales made to the government of the United States or any of its departments or agencies. . ."

This provision was enacted by Laws 1934 (Special Session), Chapter 7, Section 202. It is readily seen that there is no material difference from the exemption provision in effect today, where sales to the United States are concerned. Our Supreme Court rejected the idea that the nature of the tax, i.e. privilege tax as opposed to sales tax, could make any difference, and declined to rule on the nature of the tax. Basing its decision on the wording of the exemption statute, the Court ruled that gross receipts derived from a transaction with the United States cannot be used as the measure of **any** of the taxes imposed by the emergency school tax act. Thus, if the United States were the customer in the final retail transaction, other taxable privileges exercised prior to the retail sale were exempt from taxation. If there had been no subsequent decision of our Supreme Court in this area, we would be bound by this case.

However, in 1948, the same question came before the Court again in the case of **Black Hawk Consolidated Mines Co. v. Gallegos,** 52 N.M. 74, 191 P.2d 996. That case

involved the extraction of gold and the retail sale of that gold to the United States. The same arguments were advanced, namely that none of the taxes levied by the emergency school tax act could be applied to the receipts from the sale of gold to the United States. Again, the state argued that the exemption extended only to the privilege of selling at retail, not to the privilege of extracting gold. In 1948, a different exemption provision was in effect, being Section 72-1405, N.M.S.A., 1941 Compilation, which read as follows:

"None of the taxes levied by this act shall be construed to apply to sales made to the government of the United States or any agency or instrumentality thereof, except a corporate agency or corporate instrumentality, nor to sales to the State of New Mexico or any of its political subdivisions; provided that deposits of gold and silver with the United States' mint shall not be considered as sales to the government of the United States and shall not be exempt hereunder; nor shall such taxes apply to any businesses or transactions exempted from taxation under the Constitution of the United States or the state of New Mexico."

The efficacy of the legislature's declaring that deposits of gold with the United States mint were not sales is doubtful. The cases at that time held such deposits were, in effect, sales. See **Walling v. Haile Gold Mines,** 136 F.2d 102; and **Luke v. East Vulture Mining Co.,** 47 Ariz. 220, 54 P.2d 1002. Nevertheless, such "sales" were not included within the statutory exemption.

The Court held for the first time that the school tax is a privilege tax, and not a sales tax, noting that it had previously been erroneously denominated a sales tax in **Albuquerque Broadcasting Co. v. Bureau of Revenue,** 51 N.M. 332, 184 P.2d 416; and **Iden v. Bureau of Revenue,** 43 N.M. 205, 89 P.2d *{*333}* 519. The Court also noted that the nature of the tax had not been determined in **Gallup American Coal Co. v. Beall,** 39 N.M. 188, 43 P.2d 927.

The mining company raised the defense that the tax was imposed on a sale to the United States. This did not raise the defense of exemption, it raised the defense of immunity, without regard to exemption. The mining company relied on **Panhandle Oil Co. v. Mississippi,** 277 U.S. 218, 48 S. Ct. 451, 72 L. Ed. 857, which held invalid a state tax on the sale of gasoline to the United States Navy. The mining company also relied on **Graves v. Texas Co.,** 298 U.S. 393, 56 S. Ct. 818, 80 L. Ed. 1236, which held invalid a storage tax imposed on gasoline sold to the United States. Our Supreme Court noted that these cases had been, in effect, if not expressly, overruled by **Alabama v. King & Boozer,** 314 U.S. 1, 62 S. Ct. 43, 86 L. Ed. 482, but said of them anyway, at 52 N.M. 85:

"These cases are cited upon the assumption that the gold in question was taxed. As we have held that the tax was upon the privilege of mining, they have no application."

This crucial determination that the tax was upon the privilege of mining leads us to the opinion that such a tax is valid, even though the minerals are subsequently sold to the

United States, and that sale is exempted by statute. The **Black Hawk** case did not expressly overrule the **Gallup Coal** case, but, in our opinion, the **Gallup Coal** case is no longer sound authority, and has been, in effect, overruled by the **Black Hawk** case. Justices Sadler and McGhee, in dissent, speaking of the **Gallup Coal** case state:

"The majority notice this case and obviously overrule it in the opinion filed."

We agree that the case is overruled. As stated earlier, that case was decided less than a year after the enactment of the school tax act. No one had any broad understanding of the nature of the tax. The Court itself thought the nature of the tax immaterial. In the light of experience, and in the light of such cases as **Stone v. Green Lumber Co.,** supra, we are in a better position today to appraise the nature and operation of a privilege tax. When that appraisal is made, it is our opinion that the gross receipts derived from a sale of tangible personal property in interstate commerce, or to one of the exempt entities specified in Section 72-16-5, are exempt only from the taxes imposed by Sections 72-16-4.5 and 72-16-12, and are not exempt from the taxes that are imposed on other business activities exercised separate from or prior to the final retail transaction.

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