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1 **IN THE COURT OF APPEALS OF THE STATE OF NEW MEXICO**

2 Opinion Number: _____

3 Filing Date: June 17, 2024

4 **No. A-1-CA-39961**

5 **APACHE CORPORATION AND**
6 **SUBSIDIARIES,**

7 Protestant-Appellant,

8 v.

9 **NEW MEXICO TAXATION & REVENUE**
10 **DEPARTMENT,**

11 Respondent-Appellee.

12 **APPEAL FROM THE ADMINISTRATIVE HEARINGS OFFICE**

13 **Brian VanDenzen, Chief Hearing Officer**

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1 **OPINION**

2 **BUSTAMANTE, Judge, retired, sitting by designation.**

3 {1} This case presents multiple issues related to corporate income taxation under
4 New Mexico’s Corporate Income and Franchise Tax Act (the CIT), NMSA 1978
5 §§ 7-2A-1 to -31 (1981, as amended through 2024).¹ The dispositive issue is whether
6 Apache Corporation (Taxpayer)—a multinational oil and gas production
7 company—and its foreign subsidiaries can be deemed a “unitary corporation” as
8 defined in Section 7-2A-2(Q). The Administrative Hearing Officer (AHO)
9 concluded that the foreign subsidiaries could be included in the unitary corporation
10 as a matter of statutory definition and factual circumstance. Concluding that the
11 statutory definition excludes foreign subsidiaries not engaged in trade or business in
12 the United States as a matter of law, we reverse.

13 **BACKGROUND**

14 {2} Taxpayer is a publically traded, multinational corporation engaged in the
15 business of petroleum and natural gas exploration and production with its primary
16 offices located in Houston, Texas. Prior to 2015, Taxpayer conducted its business
17 through domestic and foreign subsidiaries. The foreign subsidiaries consisted of
18 holding companies, financing companies, and exploration and production entities

¹All reference to Sections 7-2A-1 to -31 in this opinion are to the 2015 version of the CIT unless otherwise noted.

1 incorporated and operating in Australia, Egypt, Canada, Argentina, and the United
2 Kingdom. During the relevant tax year, Taxpayer’s foreign subsidiaries paid
3 dividends, generated Subpart F income, or otherwise generated check-the-box
4 income attributed to and partially reported by Taxpayer on its 2015 federal tax
5 return. This appeal concerns only the income attributed to Taxpayer’s foreign
6 subsidiaries.

7 {3} In March 2017, the New Mexico Taxation and Revenue Department (the
8 Department) issued a notice of assessment of corporate income tax for the 2015
9 reporting period to Taxpayer. Taxpayer timely protested the assessment in June
10 2017. The protest asserted a number of grounds, including: (1) the foreign source
11 dividends were not unitary income apportionable to New Mexico; (2) the foreign
12 source dividends were not business income apportionable to New Mexico; (3) New
13 Mexico’s treatment of foreign dividends was discriminatory and thus
14 unconstitutional; and (4) assessment of penalties was not supportable. A year later
15 Taxpayer filed a supplemental protest arguing for the first time that Section 7-2A-
16 2(Q) excluded foreign corporations incorporated in a foreign country and not
17 engaged in trade or business in the United States from the definition of a “unitary
18 corporation” for all purposes under the CIT.

19 {4} After a four day hearing before the AHO, the parties filed proposed findings
20 of facts and conclusions of law and written closing arguments. The AHO issued a

1 lengthy decision and order ruling—in relevant part—that Taxpayer and its foreign
2 subsidiaries amounted to a unitary corporation under Section 7-2A-2(Q). The AHO
3 in turn concluded that the dividends paid to Taxpayer by its foreign subsidiaries and
4 other income attributed to Taxpayer were subject to the CIT. The AHO also
5 concluded that the Department’s apportionment methodology reasonably and fairly
6 calculated how much of the foreign dividends were subject to the tax. Taxpayer
7 appeals.

8 **DISCUSSION**

9 {5} On appeal from the decision and order of an AHO, we may reverse only if it
10 is “(1) arbitrary, capricious or an abuse of discretion; (2) not supported by substantial
11 evidence in the record; or (3) otherwise not in accordance with the law.” NMSA
12 1978, § 7-1-25(C) (2015); *Stockton v. N.M. Tax’n & Revenue Dep’t*, 2007-NMCA-
13 071, ¶ 8, 141 N.M. 860, 161 P.3d 905. New Mexico’s taxation scheme imposes a
14 presumption that “[a]ny assessment . . . made by the [D]epartment is . . . correct.”
15 NMSA 1978, § 7-1-17(C) (2007, amended 2023). However, when we are presented
16 with a question of law—such as the proper interpretation of a statute—we apply the
17 traditional de novo standard of review. *TPL, Inc. v. N.M. Tax’n & Revenue Dep’t*,
18 2003-NMSC-007, ¶ 10, 133 N.M. 447, 64 P.3d 474. When applying the de novo
19 standard, courts are not bound by a hearing officer’s legal interpretations or
20 conclusions. *Id.*

1 {6} Generally, “[i]n construing the language of a statute, our goal and guiding
2 principle is to give effect to the intent of the Legislature.” *Lujan Grisham v. Romero*,
3 2021-NMSC-009, ¶ 23, 483 P.3d 545. “In determining legislative intent, [appellate
4 courts] look to the plain language of the statute and the context in which it was
5 enacted, taking into account its history and background.” *Pirtle v. Legis. Council*,
6 2021-NMSC-026, ¶ 14, 492 P.3d 586. Moreover, “[w]e consider all parts of the
7 statute together, reading the statute in its entirety and construing each part in
8 connection with every other part to produce a harmonious whole.” *Dep’t of Game &*
9 *Fish v. Rawlings*, 2019-NMCA-018, ¶ 6, 436 P.3d 741 (alterations, internal
10 quotation marks, and citation omitted).

11 {7} Taxpayer argues that the AHO’s construction of the statutory definition of
12 “unitary corporation” codified in Section 7-2A-2(Q) was wrong. We have conducted
13 a reasonably comprehensive survey of relevant case law and prior AHO orders
14 dealing with unitary corporations. Our review has not uncovered any instance where
15 a similar argument has been made. We are thus presented with a matter of first
16 impression. We agree with Taxpayer’s argument and explain.

17 {8} The CIT imposes a tax upon the “net income of every domestic corporation
18 and upon the net income of every foreign corporation employed or engaged in the
19 transaction of business in, into or from this state or deriving any income from any
20 property or employment within this state.” Section 7-2A-3(A). “A unitary

1 corporation that is subject to taxation under the [CIT] . . . may elect to file a
2 combined return with other unitary corporations as though the entire combined net
3 income were that of one corporation. . . . The return filed under this method of
4 reporting shall include the net income of all the unitary corporations.” Section 7-2A-
5 8.3(A). There is no question that Taxpayer is subject to taxation under the CIT. And,
6 there is no question that Taxpayer filed a combined return for the 2015 tax year.

7 {9} The question is whether Taxpayer’s foreign dividend income is taxable by
8 New Mexico. The answer to that question under federal constitutional requirements
9 depends on whether Taxpayer and its foreign subsidiaries can be deemed unitary
10 corporations. *See Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159 (1983)
11 (discussing generally the history and development of the United States Supreme
12 Court’s case law concerning the ability of states to tax extraterritorially derived
13 income of corporations and approving California’s taxing scheme taxing dividend
14 income received from foreign subsidiaries). Whether Taxpayer and its foreign
15 subsidiaries can be treated as “unitary corporations” in turn depends on the meaning
16 of Section 7-2A-2(Q).

17 {10} Section 7-2A-2(Q) defines “unitary corporation” as
18 two or more integrated corporations, other than any foreign corporation
19 incorporated in a foreign country and not engaged in trade or business
20 in the United States during the taxable year, that are owned in the
21 amount of more than fifty percent and controlled by the same person
22 and for which at least one of the following conditions exists:

1 (1) there is a unity of operations evidenced by central
2 purchasing, advertising, accounting or other centralized services;

3 (2) there is a centralized management or executive force and
4 centralized system of operation; or

5 (3) the operations of the corporations are dependent upon or
6 contribute property or services to one another individually or as a
7 group.

8 Section 7-2A-2(Q) includes three elements; two that must be present and one that
9 acts as a carve-out provision excluding a class of entities from the definition. The
10 positive requirements are: (1) the corporations “are owned in the amount of more
11 than fifty percent and controlled by the same person,” *id.*, and that (2) the
12 corporations satisfy the “three unities test.” Section 7-2A-2(Q)(1)-(3). The three
13 unities test—detailed in the numbered subparagraphs of Section 7-2A-2(Q)—is used
14 to determine whether the state taxation of extraterritorial income of a business
15 operating in interstate commerce meets the due process requirements of the federal
16 constitution. *See Exxon Corp. v. Wisconsin Dep’t of Revenue*, 447 U.S. 207, 219-
17 223 (1980) (including as factors in the constitutional analysis “functional
18 integration, centralization of management, and economies of scale” (internal
19 quotation marks and citation omitted)).

20 {11} The third element of Section 7-2A-2(Q) is negative; that is, it excludes from
21 the definition of “unitary corporations” “any foreign corporation incorporated in a
22 foreign country and not engaged in trade or business in the United States during the

1 taxable year.” In keeping with the plain language approach to statutory
2 interpretation, the most natural interpretation of this simple and straightforward
3 language is that foreign subsidiaries of corporations subject to taxation in New
4 Mexico are not to be included in the unitary corporate group for purposes of
5 apportionment of income even if they meet the two positive qualifications. *See High*
6 *Ridge Hinkle Joint Venture v. City of Albuquerque*, 1998-NMSC-050, ¶ 5, 126 N.M.
7 413, 970 P.2d 599 (“[T]he plain language of a statute is the primary indicator of
8 legislative intent.” (internal quotation marks and citation omitted)).

9 {12} It has been undisputed throughout these proceedings that the fourteen
10 subsidiaries included in the Department’s assessment were incorporated in foreign
11 countries. There was a dispute before the AHO about whether they met the second
12 qualification, but in its supplemental brief filed at this Court’s request, the
13 Department conceded that the foreign subsidiaries did not engage in trade or
14 business in the United States during the taxable period. As such, Taxpayer’s foreign
15 subsidiaries should not have been included in its unitary corporation.

16 {13} The AHO analyzed the statute as follows:

17 By reading the statutory definition holistically, if the activities of the
18 foreign subsidiary satisfy the three numbered subparts of Section 7-2A-
19 2(Q), that foreign subsidiary would have substantially contributed to
20 the flow of value to the domestic corporation engaged in business and
21 trade in New Mexico. A foreign corporation’s contribution of value, as
22 demonstrated by meeting the subparts of the statute, to the domestic
23 entity engaged in New Mexico business activity would necessarily

1 mean it had engaged in activity in the United States through its unitary
2 relationship with the domestic corporation.

3 AHO's conclusion of law is to the same effect: "By meeting the three statutory
4 conditions of Section 7-2A-2(Q), a foreign corporation affiliated with another
5 corporation engaged in New Mexico business activity has itself necessarily engaged
6 in unitary business activities within New Mexico and the United States."

7 {14} We disagree with the AHO's analysis because it negates the existence of the
8 carve-out. If satisfaction of the three unities test determines that a taxpayer "engaged
9 in trade or business in the United States," § 7-2A-2(Q), the carve-out would cease to
10 have any effect. So long as the three unities test was met, the foreign corporation
11 exclusion would be a nonsequitur. *See Am. Fed'n of State, Cnty. & Mun. Emps.*
12 *(AFSCME) v. City of Albuquerque*, 2013-NMCA-063, ¶ 5, 304 P.3d 443 ("Statutes
13 must also be construed so that no part of the statute is rendered surplusage or
14 superfluous." (internal quotation marks and citation omitted)). This cannot be.

15 {15} In contrast, our interpretation of the foreign subsidiary carve-out language fits
16 the history of the United States Supreme Court's jurisprudence dealing with state
17 taxation of extraterritorial income and New Mexico's response to that jurisprudence.
18 As a general principle, a state may not tax value earned outside its borders. *Conn.*
19 *Gen. Life Ins. Co. v. Johnson*, 303 U.S. 77, 80-81 (1938). That principle has been
20 substantially refined by the concept that income from interstate activities of a single
21 corporation or an integrated group of corporations can be apportioned based on

1 income attributable to the corporation’s activities within a state. *See Mobil Oil Corp.*
2 *v. Comm’r of Taxes*, 445 U.S. 425, 436 (1980) (“[T]he income of a business
3 operating in interstate commerce is not immune from fairly apportioned state
4 taxation.”). “It has long been settled that the entire net income of a corporation,
5 generated by interstate as well as intrastate activities, may be fairly apportioned
6 among the [s]tates for tax purposes by formulas utilizing in-state aspects of interstate
7 affairs.” *Exxon Corp.*, 447 U.S. at 219 (internal quotation marks and citations
8 omitted). The Due Process Clause of the Fourteenth Amendment requires “a
9 minimal connection between the interstate activities and the taxing [s]tate, and a
10 rational relationship between the income attributed to the [s]tate and the intrastate
11 values of the enterprise.” *Mobil Oil Corp.*, 445 U.S. at 436-437 (internal quotation
12 marks and citation omitted). “The requisite ‘nexus’ is supplied if the corporation
13 avails itself of the substantial privilege of carrying on business within the [s]tate.”
14 *Id.* (internal quotation marks and citation omitted). Stated more simply, “[t]he simple
15 but controlling question is whether the state has given anything for which it can ask
16 return.” *ASARCO, Inc. v. Idaho State Tax Comm’n*, 458 U.S. 307, 315 (1982)
17 (internal quotation marks and citation omitted); *see F. W. Woolworth Co. v. Tax’n*
18 *and Rev. Dep’t of New Mexico*, 458 U.S. 354 (1982) (reversing the New Mexico
19 Supreme Court and holding that New Mexico had misapplied the three unities test).

1 {16} “The linchpin of apportionability in the field of state income taxation is the
2 unitary-business principle.” *Mobil Oil Corp.*, 445 U.S at 439. “[A] relevant question
3 in the unitary business inquiry is whether contributions to income of the subsidiaries
4 resulted from functional integration, centralization of management, and economies
5 of scale.” *Container Corp. of Am.*, 463 U.S. at 179 (alterations, internal quotation
6 marks, and citation omitted). These factors are commonly referred to as the three
7 unities test. “Having determined that a certain set of activities constitute a ‘unitary
8 business,’ a [s]tate must then apply a formula apportioning the income of that
9 business within and without the [s]tate. Such an apportionment formula must, under
10 both the Due Process and Commerce Clauses, be fair.” *Id.* at 169.

11 {17} The three unities test was first adopted in New Mexico 1986 as part of a
12 significant amendment of our tax statutes. 1986 N.M. Laws, ch. 20, § 33. It is
13 reasonable to surmise that adoption of the test was prompted by the United States
14 Supreme Court’s opinions referenced above—perhaps, in particular, *F. W.*
15 *Woolworth*. See 458 U.S. at 372 (concluding that the “tax d[id] not bear the necessary
16 relationship to opportunities, benefits, or protection conferred or afforded by the
17 taxing [s]tate” and “New Mexico’s tax thus fails to meet established due process
18 standards”).

19 {18} In 1992, the United States Supreme Court was presented with a new issue. It
20 was asked to decide how the Foreign Commerce Clause—U.S. Const., art. 1, § 8,

1 cl. 3—affected state taxation of international unitary corporations. *Kraft Gen. Foods,*
2 *Inc. v. Iowa Dep’t of Revenue & Fin.*, 505 U.S. 71 (1992). In *Kraft*, the Supreme
3 Court held that the Iowa tax scheme unconstitutionally discriminated against foreign
4 commerce in that it allowed a “deduction for dividends received from domestic
5 subsidiaries, but not for those received from foreign subsidiaries.” *Id.* at 74, 79.

6 {19} *Kraft* resonated in New Mexico. In 1992, Section 7-2A-8.3(D) (1986) allowed
7 corporate taxpayers to file separate returns even if they were part of a unitary
8 corporation. Section 7-2A-8.3(B) (1986) provided “[t]he secretary shall not require
9 or permit a foreign corporation incorporated in a foreign country and not engaged in
10 trade or business in the United States during the taxable year to report through a
11 combined return.” Both of these provisions were enacted in 1983. *Compare* 1983
12 N.M. Laws, ch. 213, § 12, *with* § 7-2A-8.3 (1986). The Legislature apparently
13 recognized that the separate filing option in New Mexico similarly operated to allow
14 the deduction of domestic dividends but not foreign dividends, thus creating the
15 same problem found unconstitutional in *Kraft*. The language of Section 7-2A-8.3(B)
16 (1986)—specifically barring certain foreign corporations from filing combined
17 returns—could only have exacerbated the *Kraft*-related issues.

18 {20} The Legislature addressed the issue in its 1993 session. According to a Fiscal
19 Impact Report (FIR) prepared by the Legislative Finance Committee (LFC), H.B.
20 680 was designed to address the problem raised by *Kraft*. Fiscal Impact Report H.B.

1 680, *Significant Issues*, at 1-2 (N.M. Feb. 21, 1993). Part of the solution was to
2 eliminate the separate filing option and require unitary corporations to file on a
3 combined or consolidated basis for taxable years beginning January 1, 1993. Fiscal
4 Impact Report H.B. 680, *Significant Issues*, at 1-2. Another part of the solution was
5 to amend the definition of “unitary corporations” “to exclude foreign corporations
6 incorporated in a foreign country and not engaged in business in the United States.”
7 Fiscal Impact Report H.B. 680, *Synopsis of Bill*, at 1. The amendment of the
8 definition was described as “simply mov[ing] language from Section 7-2A-8.3.”
9 Fiscal Impact Report H.B. 680, *Synopsis of Bill*, at 1.

10 {21} On March 11, 1993, the then-secretary of the Department submitted his own
11 bill analysis and FIR on an amended version of H.B. 680. Bill Analysis and Fiscal
12 Impact Report H.B. 680 (N.M. Mar. 11, 1993). The secretary’s memorandum also
13 cited the *Kraft* opinion as the motivating factor for the suggested changes. Bill
14 Analysis and Fiscal Impact Report H.B. 680, *Administrative Impact*, at 2. Pertinent
15 to our issue, the secretary also stated that, among other things, the proposed
16 legislation included “[a]mendments to [Section] 7-2A-2 [that] change the definition
17 of ‘unitary corporations’ to exclude foreign corporations not engaged in business in
18 the U.S.” Bill Analysis and Fiscal Impact Report H.B. 680, *Description*, at 1. The
19 LFC’s FIR and the secretary’s memorandum clearly referred to Section 7-2A-8.3(B)
20 as the source of the language being moved.

1 {22} The amendments to the definition of “unitary corporations” described in the
2 FIRs were enacted by Chapter 307, Section 3 of New Mexico Laws of 1993 and
3 Chapter 309, Section 1 of New Mexico Laws of 1993.² The amendment moved only
4 part of the Section 7-2A-8.3 (1992) language quoted above to the definition section
5 of the statute. *Compare* § 7-2A-8.3(D) (1992), *with* 1993 N.M. Laws, ch. 307, § 1.
6 The explicit reporting and return references in Section 7-2A-8.3(B) were stripped
7 away. Only the language at issue in this case was moved. *Compare* § 7-2A-8.3(D)
8 (1992), *with* 1993 N.M. Laws, ch. 307, § 1, *and* § 7-2A-2(Q). As inserted into the
9 definition of “unitary corporations,” the effect of the language is just as described in
10 the LFC FIR and the secretary’s memorandum: it excludes foreign corporations from
11 the definition of unitary corporations. Fiscal Impact Report H.B. 680, *Synopsis of*
12 *Bill*, at 1; Bill Analysis and Fiscal Impact Report H.B. 680, *Description*, at 1.
13 Whether inadvertent or not, the Legislature’s language achieved a solution to the
14 *Kraft* problem: if foreign subsidiaries are excluded from the definition of “unitary
15 corporation” the dividends they pay to domestic parents cannot be included as
16 taxable income. The Department has not provided any basis for us not to enforce the
17 plain import of the language.

²Section 7-2A-8.3(B) (1992) was entirely omitted by Laws, 1993, ch. 307, § 4 and Laws 1993, ch. 309 § 2.

1 **CONCLUSION**

2 {23} For the reasons stated above, we reverse the decision and order of the AHO
3 and remand for proceedings in accordance with this opinion.

4 {24} **IT IS SO ORDERED.**

5
6 **MICHAEL D. BUSTAMANTE, Judge,**
7 **retired, Sitting by designation.**

8 **WE CONCUR:**

9
10 **JANE B. YOHALEM, Judge**

11
12 **KATHERINE A. WRAY, Judge**