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## NEW MEXICO'S EFFORT AT RATIONAL TAXATION OF HARD-MINERALS EXTRACTION\*

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Compliance with and enforcement of New Mexico's taxes on the hard-minerals extractive industry is complicated, time-consuming and expensive. This article discusses briefly the taxes New Mexico presently imposes on the extraction of hard-minerals,<sup>1</sup> describes the attempted revision of the present laws in 1969 and 1970 and examines the draft bills introduced in the 1970 New Mexico legislative session as an alternative to the present system.

In addition to state taxes which apply to all corporations, New Mexico imposes the severance tax<sup>2</sup> and the resources excise tax<sup>3</sup> upon the hard-minerals industries, administered by the Bureau of

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\*The author owes her education on this subject to Mr. Franklin Jones, New Mexico Commissioner of Revenue. Errors herein are her own.

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1. Timber and sand and gravel, although subject to the present severance and resources excise taxes, were excluded from the scope of House Bills 83-84, 29th N.M. Leg., 2nd Reg. Sess. (1970). The business practices and extractive patterns of these industries are unrelated to those of the hard-minerals extractive industry. For this reason, the taxation of timber was treated in the Timber Tax Act (House Bill 85), and sand and gravel in the Sand and Gravel Tax Act (House Bill 86). A discussion of those acts and the special problems of the timber and sand and gravel industries is beyond the scope of this article.

Further, the administration of taxation of the oil and gas industry was delegated to the Oil and Gas Accounting Commission in 1959. That Commission administers the Oil and Gas Severance Tax Act, N.M. Stat. Ann. §§ 72-19-1 *et seq.* (Repl. 1961); the Oil and Gas Conservation Tax Act, N.M. Stat. Ann. §§ 72-20-1 *et seq.* (Repl. 1961); the Oil and Gas Emergency School Tax Act, N.M. Stat. Ann. §§ 72-21-1 *et seq.* (Repl. 1961); the Oil and Gas Ad Valorem Production Tax Act, N.M. Stat. Ann. §§ 72-22-1 *et seq.* (Repl. 1961); the Oil and Gas Manufacturers Privilege Tax Act, N.M. Stat. Ann. §§ 72-23-1 *et seq.* (Supp. 1970); and the Oil and Gas Production Equipment Tax Act, N.M. Stat. Ann. §§ 72-24-1 *et seq.* (Supp. 1970). The last of these acts establishes the value of tangible property or equipment used to sever, treat or store oil and gas as nine percent of the value of gross production at the wellhead. The same approach is taken in House Bill 83 to value tangible property used in mining operations, and the 1970 amendment of the method for valuing tangible property used in mining potash. See text at note 29, *infra*.

2. N.M. Stat. Ann. §§ 72-18-1 *et seq.* (Repl. 1961).

3. *Id.* §§ 72-16A-2 *et seq.* (Supp. 1970).

Revenue under the provisions of the Tax Administration Act.<sup>4</sup> Further, a special procedure for valuation of the tangible property used in mining operations, as well as of the mineral reserves, or ore body, is set forth in N. M. Stat. Ann. § 72-6-7 (1953), administered by the Property Appraisal Department.

The severance tax, enacted in 1937, is levied upon "all natural resources products severed and saved from the soil of this state,"<sup>5</sup> excluding oil and gas. The rate imposed in the Severance Tax Act is 1/8 of one percent of "gross value" for all natural resources except potash, copper and uranium. Severance of these three resources is taxed at two and one-half, one-half, and one percent, respectively. The current rates on potash and copper were established in 1949, a period of high profits for those industries. The rate on uranium was established in 1961, at the height of the uranium boom in New Mexico.<sup>6</sup>

When the severance tax rate on potash was established, the New Mexico potash industry enjoyed a virtual monopoly of the national potash market. Since then, the immensely rich Canadian potash fields have been opened, and world prices for potash have declined nearly fifty percent since 1967. In recognition of the industry's plight, the 1970 New Mexico Legislature enacted a special tax relief package for potash producers. One section therein reduces the severance tax base for potash products from eighty to forty percent of posted field or market price.<sup>7</sup> Thus, while the severance tax rate on potash is still 2½%, the industry's severance taxes were halved by this reduction in the tax base.

The severance tax is based upon "gross value," defined in the Act as "sales value. . . at the first marketable point" less specified deductions. The expenses of hoisting, crushing and loading "necessary to place the severed product in marketable form and at a marketable place," up to a limit of fifty percent of the gross sales price may be deducted from the sales price of products having a posted field or market price. Freight charges from the moment of severance to the first sale, and the actual cost of processing or beneficiation may be deducted from the gross sales price of products which must be "processed or beneficiated" before sale. No fifty percent limitation on deductions is imposed on the second category of products. The severance tax, then, is based upon the value of gross production with certain cost deductions permitted by statute.

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4. *Id.* § 72-18-3 (Repl. 1961).

5. *Id.* § 72-18-1(A).

6. See Compiler's footnotes to *Id.* § 72-18-2(B).

7. *Id.* § 72-18-2(B)(1).

In 1959, the first Severance Tax Bonding Act was passed, authorizing the issuance of bonds and pledging a portion of the monies collected under the Severance Tax Act for the payment of principal and interest on all bonds issued.<sup>8</sup> Since then, twelve similar statutes have been enacted. The proceeds of the bond issues have been used for financing a variety of state building programs.<sup>9</sup> The issuance of these bonds has important consequences for any revision attempt, since the Contracts Clause of the United States Constitution and its subsequent interpretation<sup>10</sup> forbid any lowering of the rates imposed in the Severance Tax Act, or any lessening of the base which will impair the ability of the state to repay the severance tax bondholders.

The resources excise tax, enacted in 1966, became effective on July 1, 1967.<sup>11</sup> It is a well-drafted restatement of the Emergency School Tax Act as that Act applied to the extraction and processing of minerals, timber and sand and gravel.<sup>12</sup>

The Resources Excise Tax Act imposes a resources tax,<sup>13</sup> a processors' tax,<sup>14</sup> and a service tax<sup>15</sup> which are mutually exclusive—if one is paid, the others are not due. The rate imposed under the resources and the processors' taxes for all natural resources except timber and potash is .075%. Potash producers who do not process the severed potash in New Mexico are taxed at the rate of 3%. However, this rate has never been paid by any potash producer, since all have processing plants in New Mexico, and had them at the date of the Act's passage. Similarly, the tax rate for timber severed but *not* processed in New Mexico is .075%, while the rate for timber severed *and* processed in New Mexico is .0375%. While no reliable data exists concerning the effect of this apparent tax encouragement to process timber in New Mexico, it is not thought to be of much significance since transportation costs usually dictate sawing logs close to the point of severance regardless of state tax consequences. The service tax, imposed for the privilege of severing or processing in New Mexico "natural resources owned by another and upon the taxable value of which the resources or processors' tax has not been paid," is designed to ensure that producers who sever sand and gravel

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8. N.M. Laws 1959, ch. 323, §§ 1, 2, 5-21.

9. See N.M. Stat. Ann. §§ 72-18-29 to 47 and §§ 72-18-27.1 to .13 (Repl. 1961).

10. U.S. Const. Art. I, § 10. See notes 30 & 31, *infra*, and accompanying text.

11. See Compiler's notes to N.M. Stat. Ann. §§ 72-16A-20, -29 (Supp. 1970).

12. N.M. Laws 1959, ch. 5, § 2 and ch. 54, § 28; N.M. Laws 1959, ch. 5, § 3; N.M. Laws 1959, ch. 5, § 14; N.M. Laws 1935, ch. 73, § 206; N.M. Laws 1959, ch. 5, § 16. See Compiler's notes to N.M. Stat. Ann. § 72-16A-29 (Supp. 1970).

13. N.M. Stat. Ann. § 72-16A-23 (Supp. 1970).

14. *Id.* § 72-16A-24.

15. *Id.* § 72-16A-25.

from government owned gravel pits for use in government projects, such as highways, also pay the resources excise tax.

The tax base upon which these rates are imposed is "taxable value," defined in the Act as the sales price received for the severed product, or its reasonable value, if the product is not sold or if the sales price is not representative of the product's value.<sup>16</sup> From this amount may be deducted: (1) royalties paid to the United States or the State of New Mexico; (2) sales of natural resources to the United States or the State of New Mexico; (3) sales of natural resources to certain nonprofit organizations; and (4) the cost of any transportation outside New Mexico.<sup>17</sup> The resources excise tax, then, is also a production-based tax, with certain specified deductions allowed in determining the tax base against which rates are applied.

The mineral reserves, or ore body, and tangible property used in mining operations are valued for ad valorem tax purposes by the Property Appraisal Department, established by the 1970 New Mexico Legislature to replace the State Tax Commission.<sup>18</sup> The statute under which such properties are valued provides two methods whereby the Department may value the mineral reserves of all minerals except potash—by appraisal, under established standards,<sup>19</sup> or by deducting from the market value of natural resources produced by the mine during the preceding calendar year the "actual cost of producing and bringing the output to the surface, and of milling, treating, reducing, transporting and selling the same. . . ."<sup>20</sup> In fact, due to the difficulties of valuing ores in place, the State Tax Commission consistently used the second method, which gave this tax its denomination as the "ad valorem tax on production." This tax, then, although theoretically imposed on the property value of the ore body, is in fact computed on a base which resembles the preceding year's net income of producers of all minerals except potash.

The production from potash mineral property is valued by the Property Appraisal Department under N.M. Stat. Ann. § 72-6-7.1 (1953), part of the tax relief package enacted by the 1970 New Mexico Legislature for the potash industry.<sup>21</sup> Thus, effective Jan-

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16. *Id.* § 72-16A-22(1).

17. *Id.*

18. *Id.* § 72-25-1 *et seq.*

19. *Id.* § 72-6-7 to 9 (Repl. 1961).

20. *Id.* § 72-6-7 to 10 and 12.

21. *Id.* § 72-6-7.1(c) (Supp. 1970) provides that the statewide equalization ratio shall be applied to the valuation of production of potash mineral properties as well as to the valuation of tangible property used in mining operations. This provision was enacted by the 1970 New Mexico Legislature as part of the tax relief measure for the potash industry referred to above.

January 1, 1970, production from potash mineral property is valued at fifty percent of market value of the prior year's output. Only royalties paid to the State or the United States may be deducted from market value to derive the tax base.

The ad valorem tax on production is a third production-based tax, with allowable deductions from the value of gross production specified by statute. The value of production so determined is certified by the Department to the county assessors at 100% of the established value for all minerals except potash and placed on the tax rolls of the taxing district in which the ore body is located. The value of production of potash is, under the new statute, subject to application of the uniform assessment ratio of 33 1/3% before certification to county assessors. Local millage rates are then applied and the ad valorem tax due computed.

Section 72-6-7 provides, for all minerals except potash, that the tangible property used in mining operations must be appraised by the Property Appraisal Department to establish value. This appraised value is subject to 33 1/3% to determine the assessed value against which the ad valorem mill rates are applied.

The 1970 potash tax relief package contained in N.M. Stat. Ann. § 72-6-7.1 (A) (1970 Supp.) provides that the tangible property used in mining potash will be valued, from January 1, 1970, at 100% of the market value of the property's mineral production in the prior year, rather than by appraisal by the Property Appraisal Department. This value is also subject to the 33 1/3% uniform assessment ratio before certification to county assessors, who apply local millage rates and assess the tax due.

The amount and source of deductions to be taken from market value to establish the value of the mineral property for the ad valorem tax on production was a perpetual source of protests and hearings before the State Tax Commission; the Tax Commission's appraisal of the value of mining property was also subject to continual dispute.

The State Tax Commission operated under severe budgetary restraints. One auditor and an assistant were employed to appraise all tangible property of mining firms in New Mexico annually and audit the returns filed by mining companies for purposes of establishing the annual value of each firm's mineral production. The Commission had one full-time attorney, and the part-time services of one Assistant Attorney General to handle the legal work involved in protests and hearings, as well as the Commission's day-to-day legal work. However, the 1970 New Mexico Legislature appropriated more funds

for the operation of the Property Appraisal Department, which it is hoped will improve the administration of all ad valorem taxation functions under the Department's jurisdiction.

Thus, for all hard minerals except potash, three of the four extractive taxes imposed by New Mexico are based in some manner upon the gross sales price, or market value, of the mineral property's annual production. The severance tax, resources excise tax and the ad valorem tax on mineral production each begins with gross sales value and specifies deductions which are taken to determine the tax base, or amount against which each tax rate is applied. The ad valorem tax on tangible property used in mining operations is distinct from the ad valorem tax applied to other taxpayers and justifies treatment in any extractive tax revision attempt because the Property Appraisal Department rather than a local assessor is charged with appraising the property to be taxed.<sup>22</sup> As we have seen, the valuation of tangible property used in mining potash is valued as a percentage of gross production, just as is the valuation of production equipment used to sever oil and gas.<sup>23</sup> Thus, for these minerals, every special tax imposed upon the extractive industries by the State of New Mexico is based in some manner upon a percentage of gross sales.

The serious attempt to revamp and rationalize New Mexico's extractive tax structure was born in the maelstrom of the 1969 Legislature. Under the threat of an immediate across-the-board raise in the rates of the severance and resources excise taxes, the New Mexico Mining Association (NMMA), an organization which counts among its members the major mining firms in New Mexico, pledged to the Legislative Finance Committee to attempt in good faith to produce a draft of a rational workable revision of the present system for presentation to the 1970 Legislature. Revenue Commissioner Franklin Jones, wishing to avoid for New Mexico duplication of Minnesota's unhappy experience with extractive industry taxation,<sup>24</sup> pledged his full support and assistance. When it became apparent that the NMMA could not obtain sufficient cooperation from its members to produce the promised document, Commissioner Jones began a series of hear-

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22. It should be emphasized, however, that New Mexico is not alone in her seemingly patch-work approach to the problem of taxation of the extractive industries. For an analysis of the philosophy of subjecting the extractive industries to special taxation, and a comprehensive survey of the variety of taxes imposed by other Western states, see Comment, *Approaches to State Taxation of the Mining Industry*, 10 *Natural Resources J.* 156 (1970).

23. See N.M. Stat. Ann. § 72-6-7.1(A) (Supp. 1970); and the Oil and Gas Production Equipment Tax Act, N.M. Stat. Ann. §§ 72-24-1 *et seq.* (Supp. 1970).

24. See text at note 29, *infra*: *Approaches to State Taxation of the Mining Industry*, *supra*, note 22, at 168; and Weaton, *A History of Minnesota Mining as Influenced by Taxation*, in Symposium on Mine Taxation, University of Arizona 7-1 (1969).

ings with representatives from the major New Mexico hard-minerals producers in August, 1969. A first draft was produced by mid-October and circulated to interested parties. The remainder of this article describes the bills which were prepared for presentation to the New Mexico Legislature as alternative measures—House Bills 83 and 84.<sup>25</sup>

The Professional Tax Study Committee established the principles which guided the 1969-70 revision attempt in the Committee's report to the 1969 Legislature.<sup>26</sup> The goals set by the Committee for the revision of extractive industries taxation include:

1) *Maximum revenue for the state without disadvantaging New Mexico industries in their competitive markets.*

One of the goals of any tax is obviously to produce state revenues. However, there exists a point at which the state tax burden on any given taxpayer or industry will tend to injure its competitive position, causing it to curtail operations or in extreme situations, to shut down entirely. Every payroll dollar spent in New Mexico generates up to an additional five dollars in sales in the local economy (the so-called "rollover factor"<sup>27</sup>). Because state income and gross receipts taxes on these "rolled-over" dollars provide far more state tax revenues than would a higher tax rate on a given taxpayer or industry, the Professional Tax Study Committee believed that the rates in a new tax bill should be established at a point which would generate the greatest amount of tax dollars while not harming the competitive position of New Mexico industry.

The importance of this principle was demonstrated by the introduction of Senate Bill 910 on February 4, 1969. This legislation would have provided for a five percent federal severance tax upon "gross income from the property," as defined in § 613 of the 1954 Internal Revenue Code; amounts paid as state severance taxes were allowed as credits against the federal severance tax due.<sup>28</sup> Senator Metcalf (D-Montana) stated in his introductory remarks that the pur-

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25. H.B. 83-84, 29th N.M. Leg., 2nd Reg. Sess. (1970).

26. New Mexico Legislative Council Service, *A Program for Tax Revision in New Mexico*, Vol. I at 42, and Vol. IV at 9-12. This report was published by, and is available through, the Legislative Council Service, Capitol Building, Santa Fe, New Mexico. Bureau of Revenue Commissioner Franklin Jones served as a member of the committee while engaged in private practice in Albuquerque, New Mexico.

27. A. Blumfeld et al. *A Preview of the Input-Output Study*, 18 *New Mexico Business*, Oct. 1965 at 18.

28. 115 Cong. Rec. 2583 (1969) (remarks of Senator Metcalf). However, the concept of Senator Metcalf's legislation cannot be successfully implemented until local ad valorem taxes are included within its scope. These vary so greatly that a federal law which aims to promote uniformity in state extractive taxes must take them into account or fail in its goal.



pose of the bill was to provide a new source of state revenues by encouraging the enactment of or increase in state severance taxes. Without some such encouragement, he stated, most state legislatures are reluctant to impose higher severance taxes for fear of harming the extractive industries within their states whose competitors in other states may be subject to much lower state taxes. Thus, the goal of generating maximum revenues for the State while not harming New Mexico's extractive industries can be achieved only by establishing the rates in a revised extractive tax at points which are neither substantially higher nor lower than the rates in comparable taxes imposed by states with similar resources.<sup>29</sup>

2) *Encourage the economic development of the state.*

The role of state tax policy in attracting industry is difficult to substantiate except with extreme examples. However, such examples do provide parameters for legislative action. It is generally acknowledged that Minnesota, by drastically increasing extractive industry taxation, so discouraged further investment that it was not until the passage of an amendment to the state constitution providing that no additional taxes could be imposed on the extractive industries for 25 years that firms were willing to invest the capital to develop a newly-discovered taconite ore body. Within two years after passage of the amendment, \$500 million had been invested in developing a taconite industry in the state.<sup>30</sup> At the least, then, a state hoping to stimulate capital investment by mining firms must establish a stable and rational tax policy. Further, Canada has had a measure of success with a tax incentive program for attracting extractive industries, although it must be recognized that the richness and structure of the deposits also provide incentive.

The value of mining companies in the economy of a small state is obvious. Silver City, Grants and Raton were built largely around employment the mines provide, and the entire economic climate of the state is boosted by increased mining activity. In recognition of this fact, the Professional Tax Study Committee suggested that a revised extractive industries tax contain a reduced rate of tax for firms with low net income for the tax period to encourage the beginning or continued operations of marginal producers.

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29. The difficulty of obtaining data concerning comparable tax burdens per ton of product imposed by other states is discussed in the text accompanying note 49, *infra*.

30. Montague, *The Taxation of Iron Ore in Minnesota: The Industry Viewpoint*, in Proceedings of the Forty-Fifth Annual Conference on Taxation of the National Tax Association 580, 582 (1952).

3) *Accommodation to exigencies created by the existing tax structure.*

The brief review of New Mexico's present extractive tax structure at the beginning of this article affords a glimpse of the reliance of both local and state governments upon the present taxes. State severance tax bonds have been issued to finance a multitude of state building programs, and local governments have issued ad valorem tax bonds in reliance upon revenues generated in part by the ad valorem taxes paid by mining firms. Thus, three major areas with which any revision effort must deal are the severance tax base and rates, the ad valorem tax on mineral production, and the ad valorem tax on tangible property used in mining operations.

Article 1, Section 10 of the United States Constitution provides: "No state shall . . . pass any Law impairing the Obligation of Contracts . . ." <sup>31</sup>

It has long been established that bonds issued by a state or political subdivision are contracts between the state or subdivision and the bondholders, and that such contracts are within the protection of the Contracts Clause of the Federal Constitution.<sup>32</sup> Therefore, a state law which unreasonably impairs the ability of the state to perform its contract with bondholders, by, for instance, drastically lowering tax rates upon which bonds are based, will be declared an unconstitutional impairment of the obligation of contracts.

There are two fairly standard means of avoiding an attack on constitutional grounds which are open to the draftsman of an extractive tax revision effort. One is to include a clause providing that if revenues from the stated source prove insufficient to pay bondholders, payment will be made from general state funds. Such provisions generally preclude successful attacks under the Contracts Clause since the contracts between the state or local government and bondholders will be fulfilled, even though the revenues are derived from a different source.<sup>33</sup>

A second means of avoiding constitutional attack is available because the Contracts Clause has been interpreted as forbidding only "unreasonable" impairment of the obligations of contracts.<sup>34</sup> Thus, if a tax revision which lowers rates or bases will nevertheless generate sufficient revenues to repay bonds outstanding on the date of

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31. U.S. Const. Art. I, § 10.

32. *Seibert v. Lewis*, 122 U.S. 284 (1887); *Mobile v. Watson*, 116 U.S. 289 (1886).

33. Annot., 135 A.L.R. 1287 (1941).

34. Annot., 156 A.L.R. 1264 (1945).

passage, it will not be held an impairment of the obligations of contracts.

a) *Severance tax rates and base.*

As noted earlier, twelve Severance Tax Bonding Acts have been passed by the New Mexico Legislature since 1959 which authorize the issuance of severance tax bonds and pledge for their repayment a portion of the monies collected under the Severance Tax Act. These outstanding bonds prevent the enactment of any severance tax revision which so lowers the rates or base of the severance tax that the revenue source upon which the outstanding bonds were issued is impaired.

Because of the impediment to changes in the tax structure which the use of this tax as a bonding base creates, it is suggested that the New Mexico Legislature consider utilizing a different bonding base in the future.

b) *Ad valorem tax on mineral production.*

The market value of the prior year's production, less specified deductible costs, determines the valuation placed on an ore body, or mineral reserves, by the Property Appraisal Department for ad valorem tax purposes. This valuation is certified to county assessors, who put it on the tax rolls of the taxing district in which the ore body is located. Many such taxing districts have issued ad valorem tax bonds pledging as a portion of the repayment the monies derived from the ad valorem tax on mineral production. Further, budgets and mill levies have been established in reliance on revenues from this tax. Therefore, any revision attempt must contain a method whereby approximately the same amount of money will be returned to taxing districts as long as local governments are expected to provide essential educational services, under a new extractive tax statute as the districts presently receive.

c) *Ad valorem tax on tangible property used in mining.*

The assessed value of tangible property used in mining operations is certified by the Property Appraisal Department to the county assessors, who place such values on the tax rolls of the taxing districts in which the tangible property is located—quite often different districts from those in which the ore bodies are located and on the rolls of which the ad valorem values of production have been placed. Again, the districts presently receiving ad valorem tax monies from these sources have issued ad valorem tax bonds, pledging as a portion of the repayment the monies derived from the ad valorem tax on

tangible property used in mining, and budgets and mill levies have been established in reliance upon its continued receipt. A revision effort must therefore devise a method for returning approximately the same amount of money to these local districts which they receive under the present system, until another source of revenue for the services now provided by local governments is utilized.

4) *Administrative feasibility.*

The complexity of the present tax structure, when considered with the relatively small amounts of revenue generated by hard-minerals taxation, the personnel shortage suffered by the Bureau of Revenue and the Property Appraisal Department, and the long training and expertise required to properly audit large mining firms, make the enactment of a simple, workable tax system, easily audited and readily understood by both taxpayers and administrators highly desirable, if not imperative.

5) *Economic neutrality between competing New Mexico firms and between New Mexico firms and their competitors in other states.*

Although the Professional Tax Study Committee was silent on the subject, Commissioner Jones emphasized throughout the hearings and drafting process the importance of the economic neutrality of the tax structure of the State of New Mexico. Economic neutrality has two principal facets: the State should not, through its tax structure, be the instrument whereby one New Mexico firm gains an advantage over a New Mexico competitor; nor should the State by its tax structure, subsidize inefficient New Mexico firms in the national or world-wide market place when their competitors operate without subsidization.

A gross sales-based tax, regardless of deductions allowed, penalizes the severer of natural resources for processing those resources in the state in which they are severed. This point may easily be illustrated with a description of the operations of Kennecott Copper Corporation and Phelps-Dodge Incorporated in New Mexico. Phelps-Dodge, at its Tyrone plant, extracts copper ore and processes it in New Mexico to copper ore concentrate. The concentrate is then shipped to Bisbee, Arizona for smelting and further processing. Under the present tax law, Phelps-Dodge pays the resources excise tax based upon the gross sales value, less deductions allowed, of the copper ore concentrate it sells during each tax period. Kennecott also extracts copper in New Mexico, and processes it in the state to copper ore concentrate. However, Kennecott then smelts and processes the concentrate into fire-refined copper at its Hurley, New Mexico plant.

Kennecott pays the resources excise tax based upon the gross sales value, less allowable deductions, of the fire-refined copper it sells during each tax period. Since fire-refined copper has greater sales value than copper in ore concentrate form, Kennecott, under the present system, pays relatively higher New Mexico taxes per ton of copper severed than does its competitor Phelps-Dodge. The first facet of economic neutrality, then, dictates the use of a *tax base* for each separate mining industry which will not advantage one New Mexico firm over its New Mexico competitors.

The second facet of economic neutrality is the recognition that the adoption by New Mexico of significantly lower taxes than those imposed by other states which tax extractive industries competing for the same markets, amounts to a tax subsidy of New Mexico mining companies by the State. Such a subsidy may be desirable for other reasons—to encourage the State's economic development, for instance—but it is, and should be recognized as, a subsidy by New Mexico taxpayers to New Mexico mining firms. To the extent that this maintains inefficient firms in business longer than the economics of the marketplace would otherwise dictate, such a subsidy is undesirable because it encourages the uneconomic allocation of resources.

House Bills 83 and 84<sup>35</sup> incorporate the objectives established by the Professional Tax Study Committee. A brief explanation of the structure of these bills follows.

As we have seen, the existing tax structure creates strong demands upon one who would devise a new system for taxation of the extractive industries. The obligations on the severance tax bonds must be maintained and the local governments which, in reliance on the ad valorem taxes on production and tangible personal property, have issued bonds and made budgets must be supported. To meet these demands, each bill contains four separate taxes, three of which replace the present severance tax, ad valorem tax on production, and ad valorem tax on tangible property used in mining operations. The fourth tax in each bill consumes, in a sense, the other three, since the amounts paid during the tax year for the first three may be credited against the amount due for the fourth. Although four new taxes may sound as complicated as four present ones, the tax base utilized for each of the proposed taxes is exactly the same, and will already have been computed for federal income tax purposes by mining taxpayers. Each of the three present taxes, as we have seen, is computed on a different tax base, which is used for no other purpose, and the fourth, the ad valorem tax on tangible property used in mining operations was the subject of continual dispute between mining tax-

35. H.B. 83-84 *supra*, note 25.

payers and the State Tax Commission. The tax base used in the draft bills is that contained in § 613 of the Internal Revenue Code,<sup>36</sup> which provides for the computation of the federal depletion allowance deduction by mining taxpayers. Because the features of § 613 are unfamiliar to many, and because it has never been used as a basis for state taxation of the extractive industries, its provisions merit attention here.<sup>37</sup>

The depletion allowance deduction is, like any other federal tax deduction, subtracted from gross income to arrive at taxable income for federal income tax purposes. To determine the amount of the deduction, however, the mining taxpayer computes, for each separate mining property, two sets of income figures used for no other purpose. These figures are "gross income from mining" and "taxable income from the [mining] property," as defined in § 613(c) and its accompanying regulations. The percentage of "gross income from mining" which may be deducted to arrive at federal taxable income varies for different minerals. The amount so deducted, however, may not exceed 50% of "taxable income from the property." Since the depletion percentage for each mineral is fixed by statute, a larger depletion allowance deduction may be gained by mining taxpayers only by reporting to the Internal Revenue Service "gross income from mining" and "taxable income from the property" figures which are as high as can possibly be justified. The resulting benefits of § 613 as a state tax base need hardly be stressed.

The content of "gross income from mining" is very specifically set forth in § 613(c) of the Code and § 1.613-3 of the Treasury Regulations. The figure may include income derived from extracting ores from the ground—processes defined in the Code as "mining processes"—and transportation from the mine to the processing plants or mills not in excess of 50 miles.<sup>38</sup> Of these three components, the most important is the definition contained in § 613(c) of "treatment processes considered as mining." The five minerals of the greatest economic importance to New Mexico are copper, molybdenum, potash, coal and uranium. The provisions concerning "treatment processes considered as mining" for these minerals are:

A) In the case of coal—cleaning, breaking, sizing, dust allaying, treating to prevent freezing, and loading for shipment . . .

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36. 26 U.S.C. § 613 (1964).

37. 26 U.S.C. § 613 was proposed for use as the tax base of a federal severance tax in a bill introduced by Senator Lee Metcalf (D.-Montana). See discussion at note 27, *supra*.

38. 26 U.S.C. § 613(c)(2) (1964). This provision explicitly provides that the Secretary of the Treasury may allow transportation costs in excess of fifty miles if he finds that "the physical or other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills."

C) In the case of iron ore, bauxite, ball and sagger clay, rock asphalt and ores in minerals which are customarily sold in the form of a crude mineral product (including molybdenum)—sorting, concentrating, sintering and substantially equivalent processes to bring to shipping grade and form, and loading for shipment;

D) In the case of lead, zinc, gold, silver or fluorspar ores, potash and ores or minerals which are not customarily sold in the form of crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic or magnetic), cyanidation, leaching, crystallization, precipitation (but not including electrolytic deposition, roasting, thermal or electric smelting or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore or the mineral or minerals from other material from the mine or other natural deposit . . . .<sup>39</sup>

Thus, the income attributable to production of the following products from these five minerals may be included in computing “gross income from mining”:

Copper—ore concentrates  
 molybdenum—molybdenum concentrates  
 potash—sulfate of potash magnesia  
 coal—cleaned, sized and broken coal  
 uranium—U<sub>3</sub>O<sub>8</sub> or “yellowcake”

As we have seen, a gross-sales-based tax can result in penalizing a taxpayer who processes further in New Mexico than does his competitor because his state tax will be based upon the gross sales value of a more expensive product than that upon which his competitor’s tax is based. As is apparent from this list, use of § 613 as a model for establishing a state tax base will ensure that competing mining taxpayers are taxed upon the same tax base. Thus, under House Bills 83 and 84, Kennecott and Phelps-Dodge would pay New Mexico extractive taxes based upon the value of their sales of copper ore concentrates during the tax period. The fact that Kennecott also smelts the concentrates in New Mexico would have no state tax effect, although local property taxes would be levied upon the smelting plant, just as they are upon any manufacturing plant in New Mexico.

The value of adopting an already established and much litigated tax base for use by a small state with limited tax administrative resources cannot be overemphasized. Long years of litigation between the Internal Revenue Service and mining taxpayers have settled many questions in defining the precise meaning of “gross income from mining.” The issue, for instance, of defining the market

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39. 26 U.S.C. § 613(c)(4)(A), (C), and (D).

value of coking coal severed and used in the blast furnaces of the severer with no significant sales made has been settled in litigation.<sup>40</sup> This issue might have been raised in New Mexico, since Kaiser Steel mines coal in Raton and ships it to Fontana, California for use in Kaiser's blast furnaces there, with few sales of the coal to third parties ever made. Similar questions concerning the scope of "treatment processes considered mining" for many ores and processes have also been settled after years of expensive litigation, and New Mexico can, by use of § 613, avoid much litigation of questions which are inevitably left unresolved by a new taxing statute.

The first three taxes in each bill are based on "gross income from mining" as used in § 613 and would replace the present severance tax and the ad valorem taxes on production and tangible property used in mining operations. The fourth tax in each bill, the "resources excise tax," is a percentage of gross income from mining but in no case is to exceed 20% of § 613 "taxable income from the property." The final gross income rate includes the other three taxes imposed in each bill, since amounts paid on those three during the tax year may be credited against the amount of the final tax due.

Limiting the total tax to § 613 "taxable income from the property" is intended to provide a degree of tax relief to firms which report low net income figures, for any reason, for a particular tax year. The provision is an attempt to encourage new mining development in New Mexico with a promise of somewhat lower taxes in a start-up period when net income figures are likely to be poor. It is intended also to encourage the continued operation of any marginal producer, in recognition of the fact that the "rolled-over" payroll dollars will generate far more in gross receipts and income taxes for the state's coffers than would the imposition of slightly higher taxes upon a particular mining taxpayer. However, such tax relief is simply a state subsidy of the sort discussed earlier, and the economic arguments against such subsidies apply against this one as well.

The percentage limitation contained in the bill is based on § 613 "taxable income from the property," computed by mining taxpayers to determine the 50% limitation upon the depletion allowance deduction.<sup>41</sup> Because mining taxpayers seek a depletion allowance

40. See *Woodward Iron Company v. Patterson* 59-1 U.S.T.C. 9454 (1959) wherein the court held that the representative market or field price of a like kind product should be used to determine gross income from the taxpayer's coal mining property for depletion allowance purposes. See also *Kaiser Steel Corp. v. United States* 66-1 U.S.T.C. 9457 (1966).

41. The I.R.S. limitation of the deduction which may be taken to 50% of "taxable income from the property," a net income figure, is entirely logical. If a company's net income position is poor, it is likely that the total federal taxable income will be low; the limitation, based on set income, on the depletion allowance deduction prevents such taxpayers from taking a large depletion deduction in a year when net income will be low. In



deduction as large as can be justified, the income figure here, as in "gross income from mining," tends to be high.

The Treasury Regulations<sup>42</sup> set forth the scope of deductions which must be taken in computing "taxable income from the property." These deductions include administrative and financial overhead, operating expenses, selling expenses, depreciation, taxes, and losses attributable to the mineral property upon which depletion is claimed and to income included in depletable gross income. Expenses attributable to both the mineral property upon which depletion is claimed and to other business activities are to be fairly apportioned between the two.

Again, years of litigation have settled many areas which might otherwise be subject to question in a new tax statute in defining the content of "taxable income from the property." Charitable contributions, for instance, need not be deducted,<sup>43</sup> while costs of providing employee benefits,<sup>44</sup> amounts of employee claims against the company,<sup>45</sup> and interest paid on money borrowed<sup>46</sup> must be.

House Bills 83 and 94 were presented as alternatives because of the different treatment of ad valorem taxation in each bill. The major problems in the present ad valorem tax system as it applies to the hard-minerals industries are those of valuation. As noted earlier, the numerous taxpayer protests to the State Tax Commission, now the Property Appraisal Department, concern both deductions from gross sales allowed to determine the value of production for ad valorem tax purposes, and the values established by appraising tangible property used in mining operations of all minerals except potash. House Bill 83 remedies these problems by establishing the values placed upon production and tangible property used in mining operations as a specified percentage of the previous year's § 613 "gross income from mining." The uniform assessment ratio of 33 1/3% would then be applied to both figures and an assessed value determined to be certified to county assessors as the present values are. This is precisely the approach taken by the 1970 New Mexico Legislature in revising the extractive taxes on potash. A section of that Act<sup>47</sup> provides that the value of tangible property used in mining potash shall be established by the Property Appraisal Department at 100%

other words, the depletion allowance deduction is available only to taxpayers who show some taxable net income.

42. Treas. Reg. § 1.613-4 (1968).

43. *Commissioner v. U.S. Potash Co.*, 29 T.C. 1071 (Dec. 22, 1970).

44. *Commissioner v. American Gilsonite Co.*, 259 F.2d 654 (10th Cir., 1958), *cert denied* 359 U.S. 925 (1959).

45. *Montreal Mining Co.*, 41 BTA 399 (1940).

46. *St. Mary's Oil and Gas Co.*, 42 BTA 270 (1940).

47. N.M. Stat. Ann. § 72-6-7.1(c) (Supp. 1970).

of the market value of the property's output in the prior year. The 33 1/3% uniform assessment ratio is applied to this figure, which is then certified to local assessors as the value of tangible property used in mining potash. House Bill 83, in adopting the same approach, leaves the present machinery by which ad valorem taxes are levied on the mining industry intact, replacing only the valuation *procedures* used.

Valuation of the tangible property used in mining operations as a percentage of the gross product of the mine may seem, at first glance, an artificial formula. However, the value of the tangible property used in mining is inextricably related to the value of the product which that property may be used to produce. A mine which has been shut down for three years may have on its premises exactly the same tangible property which was there three years earlier and which was appraised at a figure close to original costs. However, if the underlying ore body is now too poor or deep to be profitably mined, the tangible property is worth only what it will bring at salvage.

Valuation of tangible property as a percentage of gross product is also the approach taken in the Oil and Gas Production Equipment Tax Act.<sup>48</sup> That Act, passed in 1969, establishes the value of equipment used to treat, sever or store oil or gas as 9% of the value of the products at the wellhead, and has operated satisfactorily thus far.

House Bill 84 would dismantle the present ad valorem taxation machinery as it applies to the hard-minerals industries and replace it with taxes collected by the Bureau of Revenue at the state level. These monies would then be distributed by the Bureau to the local taxing districts in which active mineral reserves or tangible property used in mining are present in amounts roughly equal to the amounts contributed by mining taxpayers in each district.

Under both bills, the valuation of equipment and tangible property used in manufacturing operations will be left to local county assessors, as all other manufacturing valuation is. Manufacturing is defined in both bills as any processes which are non-mining processes under § 613. Thus, because smelting is a non-mining process under § 613, the income from which cannot be included in depletable gross income, the value of a smelting plant would under either bill be established by appraisal by county assessors.

The first tax in each bill, the severance tax bonding fund tax, is identical in both versions, as is the resources excise tax, the maximum tax against which the other taxes are credited.

With this in mind, a comparison of the Professional Tax Study

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48. *Id.* §§ 72-24-1 *et seq.*

Committee's stated goals with the provisions included in the bills to meet those goals is in order.

1) *Maximum revenue for the state without disadvantaging New Mexico industries in the markets in which they compete.*

Since three of the four taxes which would be paid under either alternative draft are imposed due to historical circumstances—the necessity of servicing the severance tax bonds and ad valorem tax bonds issued by local governments—the rates for these three taxes in each bill were established by comparing the historical payments made by each industry under each tax with the industry's combined § 613 “gross income from mining” in the same years. These figures were gained from depletion allowance schedules voluntarily submitted by taxpayers to the Bureau of Revenue. The rate for the maximum tax against which these three taxes are credited should, ideally, be established by information as to comparative tax burdens per ton of product imposed by the states in which New Mexico firms' competitors are located.<sup>49</sup> Such information, however, is extremely difficult to obtain. Each state imposes a variety of different taxes with different tax bases upon the minerals which are important to New Mexico's economy. Also, New Mexico firms have often had no experience with other states' extractive taxes. Thus, the maximum rate in each bill was established not by reference to the competitive circumstances of each industry, but by historical precedent. The Bureau of Revenue and New Mexico mining taxpayers are currently seeking reliable data on comparable tax burdens per ton of product imposed by other states with similar resources. If further information becomes available, the maximum rates in each bill will be altered appropriately.

2) *Encouragement of New Mexico's economic development.*

This goal was met by limiting the amount of the maximum tax due to twenty percent of each taxpayer's § 613 “taxable income from the property.” Several extractive taxpayers objected that the twenty percent limitation imposed was unrealistically high. The figure was selected because a balance had to be achieved between the desirability of giving marginal operators a “tax break” to encourage development, and the recognition that such a tax advantage is a subsidy by the state to marginal producers which may have the effect

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49. The importance of other states' tax rates was recognized by Senator Metcalf who noted that states are prohibited from imposing tax rates on the extractive industries as high as they might by lower rates in other states, which would harm their home industries' competitive positions, to the ultimate detriment of the taxing state. *See 115 Cong. Rec.* 2583 (1969).

of supporting inefficient firms. Those who quarrel with the figure selected have simply reached a different, and perhaps no less warranted, conclusion in the judgment which must be made.

3) *Accommodation to the existing tax structure.*

As we have seen, severance tax bonds authorized by the New Mexico Legislature and ad valorem tax bonds issued by local governments depend for their repayment upon future tax collections. As we have also seen, these outstanding bonds pose a possible constitutional problem in the revision of New Mexico's extractive taxes. The approach taken in House Bills 83 and 84 is to treat each of the three present taxes upon which bonds have been issued in a separate section of the new bills, in an attempt to insure that sufficient funds to repay bondholders would be generated under either bill.

a) *Severance tax.*

One section in each bill imposes a "severance tax bonding fund tax" at a rate which would yield sufficient revenues to service the bonds outstanding at the date of the Act's passage. In an additional effort to preclude a finding of unconstitutionality under the Contracts Clause, each bill contains a proviso which authorizes the State Board of Finance to transfer monies collected under the resources excise tax to the severance tax bonding fund when necessary to repay bondholders.

b) *Ad valorem tax on mineral production.*

House Bill 83 revises only the method of determining the valuation placed on mineral production by establishing the value of production as a percentage, different for each mineral, of § 613 "gross income from mining." The value so determined is subject to the uniform assessment ratio of 33 1/3%, and is then certified to local assessors. Since the percentages employed in House Bill 83 were established by reference to historical payments of this tax made by each mining industry, this approach does not raise any problem under the Contracts Clause; at least as much revenue would be returned under a revised valuation system as under the present valuation method.

House Bill 84 replaces the present ad valorem tax on production with a tax collected at the state level. In order to ensure that local taxing districts receive approximately the same amounts of ad valorem tax monies as are received under the present system, it includes a formula for returning to each taxing district a portion of the total monies collected in direct proportion to the monies contributed by mining taxpayers in that taxing district.

c) *Ad valorem tax on tangible property used in mining operations.*

Again, House Bill 83 revises only the method by which tangible property used in mining is valued, establishing that value as a percentage of § 613 "gross income from mining." This approach, as we have seen, is taken in the Oil and Gas Ad Valorem Production Equipment Tax Act,<sup>50</sup> and in the special potash tax relief act passed by the 1970 New Mexico Legislature.<sup>51</sup> The value so established is subject to the uniform assessment ratio of 33 1/3% and is then certified to local assessors.

House Bill 84 also establishes the value of tangible property used in mining as a percentage of § 613 "gross income from mining," but replaces the present ad valorem system with a tax collected at the state level and distributed to taxing districts in direct proportion to that contributed by taxpayers in their districts.

Since either bill would return to taxing districts approximately the same amounts of revenue generated by the present ad valorem tax on tangible property used in mining, neither may be attacked on the ground that it is a legislative impairment of the obligations of local governments' contracts with ad valorem bondholders.

4) *Administrative feasibility.*

Use of § 613 as a model for establishing the tax base for each tax imposed in both bills is the means whereby efficient and inexpensive administration of a new extractive tax is attained. As we have seen, litigation between the I.R.S. and mining taxpayers has answered many questions which might otherwise be the subject of expensive and protracted lawsuits between the State of New Mexico and mining taxpayers. Further, since this tax base will have been computed for federal income tax purposes, the revised bill will substantially ease the burden of compliance with state extractive tax laws.

Under the terms of an agreement between the State of New Mexico and the Internal Revenue Service, the Bureau of Revenue will have access to mining taxpayers' federal income tax returns containing federal depletion allowance schedules. As a further enforcement aid, both bills require the taxpayer to submit federal depletion allowance schedules containing computations of § 613 "gross income from mining" and "taxable income from the property" with the New Mexico year-end return.

5) *Economic neutrality.*

The goal of maintaining the economic neutrality of New Mexico's

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50. N.M. Stat. Ann. § § 72-24-1 *et seq.* (Supp. 1970).

51. *Id.* § 72-6-7.1(c).

tax structure has two principal aspects: economic neutrality between New Mexico-based competitors, and economic neutrality between New Mexico firms and out of state competitors.

The implementation of the first goal is ensured by use of § 613 as the base of a new extractive tax. As we have seen, a gross sales-based tax discriminates against the severer who also processes in New Mexico, since his tax base is the sales value of his final product—which may be more expensive than his competitors' final product. "Gross income from mining" under § 613 includes only the income from processes which are "treatment processes considered as mining" for each mineral. Thus, potash producers will pay the tax upon a base which includes only income from producing potash of sulfate magnesia, and copper producers will pay the tax from a base which includes only income from producing copper ore concentrates, regardless of any further processing or manufacturing performed in New Mexico.

The second goal—economic neutrality between New Mexico firms and their out of state competitors—can be met only by establishing the rates of the maximum tax in both bills at levels which reflect the comparable tax burdens imposed per ton of product by states which have similar resources. However, until reliable data is obtained concerning these comparative burdens, the rates would be established by historical precedent.

Several problems remain in the bills introduced in the 1970 New Mexico Legislature. The major difficult areas deserve a brief review here.

As was pointed out by many mining taxpayers, House Bills 83 and 84 use a percentage of § 613 "gross income from mining" in establishing the value of mineral production. The present ad valorem value of mineral production is determined by subtracting certain specified costs from the market value of production, which results in a figure roughly akin to net income. Use of this base affords a measure of tax relief to firms in the tax year following a year of low net income, but it also wreaks havoc upon those taxing districts and local governments which depend heavily on the ad valorem tax from production, since their revenues may be cut drastically. Because of the need to provide local governments with a measure of stability and predictability in their ad valorem tax revenues, both House Bills 83 and 84 adopt a base of gross, rather than net, income. The limitation of the maximum tax to twenty percent of § 613 "taxable income from the property" is intended to place the burden of tax relief on the state, which can better weather such fluctuations than can local governments.

A second complaint of many mining taxpayers is that the bills provide that any excess credit against the resources excise tax may only be applied to successive tax periods in the same tax year. However, the tax scheme of both bills is an annual tax, with adjustments allowed at year's end for final § 613 figures, and for refunds where excess resources excise taxes have been paid. For this reason it was felt that each tax year should stand as a single unit.

A third objection voiced by many is that a maximum tax of twenty percent of "taxable income from the property" is too high to give effective tax relief to mining firms with poor net income positions. As noted earlier, this figure was selected as the compromise between the desire to give marginal producers a tax break to encourage their continued operation and the recognition that a tax break by the state may simply be a subsidy to an inefficient firm.

A fourth point raised by a mining taxpayer merits serious attention in the redrafting which will occur in the Fall of 1970. That is the effect of the maximum tax rate contained in both bills in the year after a company has been shut down for a large portion of the year. Further work is being done to remedy the possible problem in this area.

The search for a rational scheme of taxation of New Mexico's extractive industries is far from over. Further research on the inclusion of the oil and gas industry in the present House Bills 83 and 84 will be carried on in the Fall of 1970. Further conferences between the industries and the Bureau of Revenue are needed to strengthen and improve the bill or bills to be presented to the 1971 Legislature. It is hoped that New Mexico's example, should it prove successful, will encourage other states with significant mineral resources to consider enactment of extractive taxes based on a percentage of § 613 "gross income from the property." Such statutes, or the passage of an improved version of Senator Metcalf's bill, would provide the data on comparative tax burdens necessary to establish New Mexico tax rates at points which generate maximum revenue for the state while not harming New Mexico industries in their competitive markets, and hasten the day of rational taxation of the extractive industries in New Mexico.

## Appendix

### HOUSE BILL 83

29th LEGISLATURE – STATE OF NEW MEXICO – 2ND SESSION, 1970

#### AN ACT

RELATING TO TAXATION; PROVIDING FOR THE TAXATION OF NATURAL RESOURCES; AND REPEALING SECTIONS 72-6-7, 72-16A-20 THROUGH 72-16A-29 AND 72-18-1 THROUGH 72-18-27 NMSA 1953 (BEING LAWS 1921, CHAPTER 133, SECTION 505, LAWS 1966, CHAPTER 48, SECTIONS 1 THROUGH 10, LAWS 1937, CHAPTER 103, SECTIONS 1 THROUGH 3, LAWS 1951, CHAPTER 24, SECTION 5, LAWS 1937, CHAPTER 103, SECTIONS 5 THROUGH 19, LAWS 1951, CHAPTER 24, SECTIONS 3 AND 4 AND LAWS 1937, CHAPTER 103, SECTIONS 20 THROUGH 25, AS AMENDED).

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF NEW MEXICO:

Section 1. TANGIBLE PROPERTY USED IN MANUFACTURING—ASSESSMENT.—Tangible property used in manufacturing shall be valued by appraisal and assessed as provided by law. The ad valorem tax rate for tangible property used in manufacturing shall be established as provided by law. As used in this section, “tangible property used in manufacturing” means any structure, improvements, equipment or real property used for treatment processes of natural resources not included in the definition of “mining” in Section 613 of the United States Internal Revenue Code of 1954, as amended or renumbered.

Section 2. SHORT TITLE.—This act may be cited as the “Resources Tax Act”.

Section 3. DEFINITIONS.—As used in the Resources Tax Act:

A. “bureau” means the New Mexico bureau of revenue, the commissioner of revenue or any employee of the bureau exercising authority lawfully delegated to him by the commissioner;

B. “person” means any individual, estate, trust, receiver, cooperative association, club, corporation, company, firm, partnership, joint venture, syndicate or other entity;

C. “natural resource” means any metalliferous or nonmetalliferous mineral product, but does not include oil, natural gas, liquid hydrocarbons, individually or any combination thereof, or carbon dioxide, timber or sand and gravel;

D. “Section 613” means Section 613 of the United States Internal Revenue Code of 1954, as amended or renumbered;

E. “sever” means to mine, quarry or extract any natural resource in New Mexico in which the person severing the natural resource has an economic interest;

F. “process” means treatment processes included in mining;

G. “mining” means “mining” as defined in Section 613;

H. “assessed value” means the value of mineral production or the value of tangible property used in mining operations against which ad valorem tax rates are applied;

I. “owns” includes leasing tangible property if the lessee is liable for payment of ad valorem taxes on the tangible property;

J. “tangible property used in mining operations” means any structure, improvements, equipment or real property used to sever or process natural resources in New Mexico;

K. “gross value of production” means the amount of “gross income from mining” in New Mexico as defined and used in Section 613, excluding proceeds from the sale of production payments and paybacks on production payments sold in prior years;

L. “net value of production” means the amount of “taxable income from the property” in New Mexico as defined and used in Section 613, excluding proceeds from the sale of production payments and paybacks on production payments sold in prior years;

M. “production payment” means an amount of money received in one tax year which is to be paid back in later tax years from receipts from the sale of the production of natural resource products;

N. “payback” means money or property repaid by a person who severs natural resources or processes natural resources, or both, to a person who bought the production in a prior tax year;



O. "salvage value" means ten percent of the full original installed cost of all tangible property used in mining operations;

P. "original installed cost" includes taxes, freight charges and the cost of installing tangible property used in mining operations;

Q. "tax period" means each quarter of the tax year; and

R. "tax year" means the fiscal year used by a taxpayer for federal income tax purposes.

Section 4. OPTIONAL TREATMENT AS PERSON.—A partnership, limited partnership, joint venture, syndicate or association may elect to have each of its partners, venturers or members treated as a person to the extent of his agreed interest in the partnership, limited partnership, joint venture, syndicate or association. Any partnership that elects the treatment provided for in this section shall identify each partner and the extent of his interest in the partnership to the bureau.

Section 5. METHOD OF DETERMINING ASSESSED VALUE OF PRODUCTION.—

A. By October 15 of each year, the bureau shall report to the state tax commission the gross value of production of each person severing or severing and processing natural resources in New Mexico for the previous tax year.

B. The basis of valuation of production shall be an amount equal to the following percent of the gross value of production of each natural resource for the previous tax year:

<i>Natural Resources</i>	<i>Percent</i>
Potash . . . . .	100
Coking coal . . . . .	60
Steam coal . . . . .	90
Copper . . . . .	195
Uranium . . . . .	60
Molybdenum . . . . .	90
Limestone . . . . .	75
Other natural resources . . . . .	100.

C. The assessed value of production shall be determined by applying the uniform assessment ratio to the basis for valuation of production.

Section 6. METHOD OF DETERMINING ASSESSED VALUE OF TANGIBLE PROPERTY USED IN MINING OPERATIONS.—

A. By October 15 of each year, the bureau shall report to the state tax commission the gross value of production of each person severing or severing and processing natural resources in New Mexico for the previous tax year.

B. The basis of valuation of tangible property used in mining operations shall be salvage value of the taxpayer's tangible property used in mining operations or an amount equal to the following percent of gross value of production of each natural resource for the previous tax year, whichever is greater:

<i>Natural resource:</i>	<i>Percent:</i>
Potash . . . . .	100
Coking coal . . . . .	105
Steam coal . . . . .	105
Copper . . . . .	90
Uranium . . . . .	90
Molybdenum . . . . .	105
Limestone . . . . .	30
Other natural resources . . . . .	100.

C. By regulation, the commissioner of revenue may provide for other methods for the valuation of tangible property used in mining operations for taxpayers who pay other persons to process natural resources severed by the taxpayer or who use tangible property to process natural resources severed by the taxpayer and natural resources owned and severed by other persons. The bureau shall report to the state tax commission the methods used by these taxpayers and the basis for valuation used by each taxpayer.

D. The assessed value of tangible property used in mining operations shall be determined by applying the uniform assessment ratio to the basis of valuation of tangible property used in mining operations.

E. Nothing in this section shall be construed to change the method by which tangible property used in manufacturing is valued for ad valorem tax purposes. As used in this section, "tangible property used in manufacturing" means any structure, improvements, equipment or real property used for treatment processes of natural resources, but not included in mining.

Section 7. ALLOCATION OF ASSESSED VALUE OF PRODUCTION.—If a taxpayer severs natural resources in one or more taxing districts and processes the severed natural resources in another taxing district, the assessed value of production shall be allocated to the taxing district in which natural resources were severed.

Section 8. ALLOCATION OF ASSESSED VALUE OF TANGIBLE PROPERTY USED IN MINING OPERATIONS.—If a taxpayer owns tangible property used in mining operations located in two or more taxing districts, the assessed value of the tangible property used in mining operations in each taxing district shall be determined by multiplying the taxpayer's total assessed value of tangible property used in mining operations in New Mexico by a fraction, the numerator of which is the original installed cost of the taxpayer's tangible property used in mining operations in that taxing district and the denominator of which is the total original installed cost of all the taxpayer's tangible property used in mining operations in New Mexico.

Section 9. AD VALOREM TAX LEVIED—EXCLUSIVE MEASURE OF AD VALOREM TAX LIABILITY.—

A. An ad valorem tax is levied on the assessed value of production and on the assessed value of tangible property used in mining operations of each person severing or severing and processing natural resources in New Mexico. The tax rate shall be established as ad valorem tax rates are established.

B. The tax levied by this section is the exclusive measure of the ad valorem tax liability for production and for tangible property used in mining operations of any person severing natural resources in New Mexico and is in lieu of any tax on minerals in place.

Section 10. IMPOSITION OF SEVERANCE TAX BONDING FUND TAX—DISPOSITION.—

A. For the privilege of severing or severing and processing natural resources, there is imposed on any person severing or severing and processing natural resources in New Mexico an excise tax at the following rates on the gross value of production of each natural resource for the tax period:

<i>Natural resource:</i>	<i>Rate:</i>
Potash . . . . .	0.5%
Coking coal . . . . .	0.1
Steam coal . . . . .	0.5
Copper . . . . .	0.5
Uranium . . . . .	0.5
Molybdenum . . . . .	0.1
Limestone . . . . .	0.1
Other natural resources . . . . .	0.1

B. The tax imposed by this section shall be referred to as the "severance tax bonding fund tax."

C. All revenue collected from the severance tax bonding fund tax shall be deposited to the credit of the severance tax bonding fund created by the Severance Tax Bonding Act. If the revenue collected from the severance tax bonding fund tax is not sufficient to maintain the amount of money in the severance tax bonding fund required by the Severance Tax Bonding Act, revenue collected from the resources excise tax, in the additional amounts determined by the state board of finance as necessary to maintain the required amount, shall be deposited to the credit of the severance tax bonding fund.

Section 11. IMPOSITION OF RESOURCES EXCISE TAX—LIMIT ON AMOUNT—CREDIT.—

A. For the privilege of severing or severing and processing natural resources, there is imposed on any person severing or severing and processing natural resources in New Mexico an excise tax, not to exceed twenty percent of the net value of production, at the following rates on the gross value of production of each natural resource for the tax period:

<i>Natural resource:</i>	<i>Rate:</i>
Potash . . . . .	4.0%
Coking coal . . . . .	2.5
Steam coal . . . . .	2.5
Copper . . . . .	3.5
Uranium . . . . .	2.5
Molybdenum . . . . .	3.5
Limestone . . . . .	3.5
Other natural resources . . . . .	3.0.

B. The tax imposed by this section shall be referred to as the "resources excise tax."

C. The amount of the ad valorem tax levied by Section 9 or the severance tax bonding fund tax, or both, paid or accrued during the tax period may be credited against the amount of the resources excise tax due for the same tax period. If the credit exceeds the amount of the resources excise tax due, the excess credit may be applied against the resources excise tax due for the next tax period in the same tax year.

**Section 12. OVERHEAD AND ADMINISTRATIVE EXPENSES—LIMITED DEDUCTION.—**

A. Each person liable for payment of the resources excise tax shall compute a fraction, the numerator of which is the total amount deducted during the tax years 1965 through 1969 as general overhead and administrative expenses for computation of the depletion allowance deduction for federal income tax purposes under Section 613 and the denominator of which is the total gross income from mining reported for the tax years 1965 through 1969 for computation of the depletion allowance deduction for federal income tax purposes under Section 613.

B. The amount deducted as general overhead and administrative expenses to determine net value of production shall not be more than five percent larger than an amount derived by multiplying gross value of production for the tax year by a fraction computed as provided in Subsection A.

C. General overhead and administrative expenses shall not be allocated to other expense items for purposes of the Resources Tax Act.

**Section 13. DATE PAYMENT DUE.—**The severance tax bonding fund tax and the resources excise tax shall be paid by the twenty-fifth day of the month following the end of each tax period.

**Section 14. ESTIMATE OF TAX—REPORTS—ADDITIONAL PAYMENT.—**

A. Any person liable for payment of the severance tax bonding fund tax or the resources excise tax shall estimate his gross value of production for the period upon which the tax is based and compute and pay the tax on the estimated amount. The computations of the estimated gross value of production shall be filed with the bureau when the return for the tax is filed.

B. Any person liable for payment of the resources excise tax may estimate his net value of production for each tax period and compute the limitation on the resources excise tax provided for in Section 11, for each tax period on the estimated amount. The computations of the estimated net value of production shall be filed with the bureau when the return for the resources excise tax is filed.

C. When the taxpayer files a federal income tax return for the tax year with the United States internal revenue service, he shall:

- (1) file with the bureau for the same tax year a final return for the taxes for which he is liable;
- (2) file with the bureau a copy of the federal depletion allowance return and schedule that he filed with the United States internal revenue service; and
- (3) pay any additional amount of tax that may be due or claim a refund.

**Section 15. INTEREST AND CIVIL PENALTY ON DEFICIENCIES.—**If the amount of the severance tax bonding fund tax or the resources excise tax, or both, is understated by more than fifteen percent, interest and the civil penalty for negligence, as provided in the Tax Administration Act, shall be paid to the state on any amounts exceeding the fifteen percent by which the tax was understated.

Section 16. ADMINISTRATION.—The Resources Tax Act shall be administered as provided in the Tax Administration Act.

Section 17. SCHEDULE—FILING REQUIRED.—

A. Any person severing natural resources in New Mexico shall file with the bureau a schedule showing the original installed cost of all tangible property used in mining operations in New Mexico and the taxing district in which the tangible property is located.

B. Supplemental schedules shall be filed with the bureau every six months showing the original installed cost of all tangible property used in mining operations in New Mexico which was acquired, abandoned, sold or exchanged since the last schedule was filed.

C. A schedule shall be filed within ninety days after the effective date of the Resources Tax Act or after the date a person begins severing natural resources in New Mexico.

Section 18. REPEAL.—Sections 72-6-7, 72-16A-20 through 72-16A-29 and 72-18-1 through 72-18-27 NMSA 1953 (being laws 1921, Chapter 133, Section 505, Laws 1966, Chapter 48, Sections 1 through 10, Laws 1937, Chapter 103, Sections 1 through 3, Laws 1951, Chapter 24, Section 5, Laws 1937, Chapter 103, Sections 5 through 19, Laws 1951, Chapter 24, Sections 3 and 4 and Laws 1937, Chapter 103, Sections 20 through 25, as amended) are repealed.

Section 19. EFFECTIVE DATE.—The effective date of the provisions of this act relating to potash shall be January 1, 1970. The remainder of this act shall become effective upon certification by the secretary of state that the constitution has been amended as proposed by a joint resolution of the twenty-ninth legislature, second session, entitled "A JOINT RESOLUTION PROPOSING AN AMENDMENT TO ARTICLE 8 OF THE CONSTITUTION OF NEW MEXICO BY REPEALING SECTION 1 AND ENACTING A NEW SECTION TO ALLOW CLASSIFICATION OF PROPERTY FOR THE PURPOSE OF VALUATION," but not before January 1, 1972.