STATE TAXATION ON THE GENERATION OF ELECTRICITY

HEARING

BEFORE THE

SUBCOMMITTEE ON ENERGY

OF THE

COMMITTEE ON FINANCE

UNITED STATES SENATE

NINETY-FOURTH CONGRESS

SECOND SESSION

ON

S. 1957

A BILL TO PROHIBIT STATE TAXATION ON THE GENERATION OF ELECTRICITY DISTRIBUTED IN INTERSTATE COMMERCE

MARCH 8, 1976

Printed for the use of the Committee on Finance

U.S. GOVERNMENT PRINTING OFFICE

69-529 O WASHINGTON : 1976

For sale by the Superintendent of Documents, U.S. Government Printing Office
Washington, D.C. 20402 - Price 95 cents
There is a minimum charge of $1.00 for each mail order

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STATE TAXATION ON THE GENERATION OF ELECTRICITY

MONDAY, MARCH 8, 1976

U.S. SENATE,
SUBCOMMITTEE ON ENERGY OF THE COMMITTEE ON FINANCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2 p.m., in room 2221, Dirksen Senate Office Building, Senator Mike Gravel (chairman of the subcommittee) presiding.

Present: Senators Gravel and Fannin.

Senator GRAVEL. The hearing will come to order.

I would like to welcome you to the Senate Committee on Finance Energy Subcommittee hearing on State taxation on the generation of electricity.

[The Committee on Finance press release announcing this hearing and the bill S. 1957 follows:]

Press Release

COMMITTEE ON FINANCE,
Subcommittee on Energy, Dirksen Senate Office Bldg.

SENATOR MIKE GRAVEL ANNOUNCES SUBCOMMITTEE HEARINGS ON STATE TAXATION ON THE GENERATION OF ELECTRICITY DISTRIBUTED IN INTERSTATE COMMERCE

Senator Mike Gravel (D.-Alaska), Chairman of the Finance Committee's Subcommittee on Energy, today announced that at the request of Senator Paul Fannin (R.-Arizona) the panel will conduct hearings on March 8, on S. 1957, a bill to prohibit Sate taxation on the generation of electricity distributed in interstate commerce.

The hearings will be held beginning at 2 p.m. on Monday, March 8, in Room 2221, Dirksen Senate Office Building.

Senator Fannin stated the purpose of these hearings is to determine whether the imposition of a State tax on the privilege of generating electricity in a State should be prohibited as an unreasonable burden on interstate commerce where the electricity generated is transmitted to and consumed in another State. Senator Fannin noted that this problem is primarily confined to the States of Arizona and New Mexico where Arizona power companies are subject to a discriminatory tax imposed by the State of New Mexico. However, a number of other States are viewing this matter with great interest because of its potential as an additional revenue source which may be obtained from taxpayers beyond their borders.

The following witnesses have been scheduled to appear on March 8:

Mr. Henry Sargent, Vice President—Finance, Arizona Public Service Company, Phoenix, Arizona.

Mr. B. D. Johnson, Executive Manager, Accounting and Control, Virginia Electric Power Co., Richmond, Va.

Mr. Fred L. O'Cheskey, Commissioner of Revenue, New Mexico—accompanied by Mr. Jan Unna, Assistant Attorney General, New Mexico, Santa Fe, New Mexico.

Mr. E. E. Fournace, Senior Vice President of the Ohio Power Co., Canton, Ohio.

Mr. Richard L. Dailey, West Virginia State Tax Commissioner, Charleston, West Virginia.

Senator Gravel said that the subcommittee would be pleased to receive written testimony from persons or organizations who wish to submit statements for the record. Statements submitted for inclusion in the record should be typewritten, not more than twenty-five double-spaced pages in length, and mailed with five copies by Friday, April 9, 1976, to Michael Stern, Staff Director, Senate Finance Committee, 2227 Dirksen Senate Office Building, Washington, D.C. 20510.

94TH CONGRESS
1ST SESSION

S. 1957

IN THE SENATE OF THE UNITED STATES

JUNE 17 (legislative day, JUNE 6), 1975

Mr. FANNIN introduced the following bill; which was read twice and referred to the Committee on Finance

A BILL

To amend the Act of September 14, 1959 (Public Law 86-272; 73 Stat. 555).

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Congress finds that generation of electricity and its transmission from one State to another are integral parts of interstate commerce and the imposition of a State tax on the privilege of generating electricity in a State is an unreasonable burden on commerce among the States to the extent that the electricity generated in the State is transmitted to and consumed in another State.

SEC. 2. That (a) the Act of September 14, 1959 (Public Law 86-272; 73 Stat. 555), is amended—

(1) by redesignating title II as title III, and

(2) by inserting immediately after title I the following new title:

"TITLE II—DISCRIMINATORY TAXES

"SEC. 201. (a) No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after the date of enactment of this title, a tax on the privilege of conducting interstate commerce activities within such State by any person if such tax is imposed on or with respect to the generation of electricity within such State, to the extent that such electricity is transmitted to and consumed outside of such State.

"(b) No State, or political subdivisions thereof, shall have power to assess, after the date of enactment of this title, any tax which was imposed by such State or political subdivision, as the case may be, for any taxable year ending on or before such date, on the privilege of conducting interstate commerce activities within such State by any person, if the imposition of such tax for a taxable year ending after such date is prohibited by section 201.".

(b) Title III of such Act, as redesignated by subsection (a) of this Act, is amended—

(1) by redesignating sections 201 and 202 of such title as sections 301 and 302, respectively, and

(2) by adding at the end of section 301, as redes-

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ignated by this subsection, the following new sentence: "The Committee on the Judiciary of the House of Representatives and the Committee on Finance of the United States Senate, acting separately or jointly, or both, or any duly authorized subcommittees thereof, shall make full and complete studies of all matters pertaining to the taxation by the States on the privilege of generating electricity within such States to the extent that such electricity is transmitted to and consumed outside of such States, for the purpose of recommending to the Congress proposed legislation providing uniform standards to be observed by the States in imposing taxes of such activities.".

Senator GRAVEL. This matter was brought to the Senate's attention last June by Senator Fannin when he introduced his bill, S. 1957. Today, at his request, we are holding investigative hearings on the situation that currently exists in Arizona and New Mexico and the implications that it has for energy policy throughout the Nation.

Events of the last 3 years have shown us the importance of diversifying our energy base, both in terms of energy sources and energy generation.

In the future, much importance will be placed on energy facility siting to insure that those areas that are particularly suited for the production of one kind of power are utilized to the fullest extent possible. Their power will serve both domestic energy markets and the export market.

Alaska is, perhaps, the prime example of an energy exporting State. Energy is our largest natural resource. In addition to the immense oil and natural gas fields at Prudhoe Bay, Alaska has significant potential deposits in the offshore areas of our coast, we have the Naval petroleum reserve and there are other reserves in selected areas in the interior.

We also have a significant potential for hydroelectric power at Devils Canyon. Because of our small population, nearly all energy produced here is designed for export markets.

Gentlemen, I look forward to your testimony and thank you for coming to meet with us.

At this time I would like to call on my good friend and colleague, Senator Fannin, who is really the instigator of all this, for a statement.

Senator FANNIN. Thank you, Mr. Chairman.

I want to express my appreciation to you, Mr. Chairman, for scheduling these hearings and to the Committee Chairman as well.

These hearings are particularly timely as the committee proceeds toward the markup of H.R. 10612 to which Chairman Long would like to add an energy title.

S. 1957 prohibits State taxation on the generation of electricity distributed in interstate commerce. Specifically, the bill prohibits State taxation on:

1. The generation of electricity within a State to the extent that the electricity is transmitted to and consumed outside of the State; and

2. The distribution of electricity within a State to the extent that the electricity is transmitted from outside the State and consumed within the State.

This legislation was introduced to alleviate a specific problem confronting Arizona. The problem to which I refer is New Mexico's recently enacted Electrical Energy Tax Act which became effective July 1, 1975.

This law imposes two new taxes: one on generators of electricity in New Mexico and the other on out-of-State generators doing business in New Mexico.

While at first glance this tax structure may appear to be equitable in that it purports to tax both domestic and foreign generators equally, that is, in fact, not the case due to the operation of tax credits available under the Electrical Energy Tax Act.

The law provides for a tax credit against the gross receipts tax owed New Mexico for any tax imposed by the act on electricity generated and consumed within New Mexico.

There is no credit available for any tax paid on electricity generated in New Mexico but consumed outside of New Mexico.

The practical operation and effect of these tax credit provisions of the Act shift the incidents of the Electrical Energy Tax from the generation of electrical energy to the interstate transmission of electrical energy outside New Mexico.

Mr. Chairman, the Four Corners Generating Plant near Farmington, New Mexico, is owned by six participants and provides energy to four States plus two others in times of emergency.

Those states are New Mexico, Texas, Arizona and California, plus Utah and Nevada. Three of the six participants are Arizona Public Service Company, Tucson Gas and Electric Company and the Salt River Project.

Massive amounts of electricity are transmitted from the Four Corners Generating Plant to Arizona. This type of joint venture plant has been built and additional ones are on drawing boards or in the beginning stages of construction.

In addition to the Four Corners Generating Plant, there presently are in existence the Navajo Plant at Page, Arizona, owned by six participants which provides energy to Nevada, Arizona and California as well as the Mohave Plant in eastern Nevada owned by four participants which provides energy to California, Arizona and Nevada.

Mr. Chairman, New Mexico's electrical energy tax is imposed entirely on out-of-State consumers of electricity generated in New Mexico.

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Allowing this tax to continue in force would be an injustice to the State of Arizona and other States in the Western United States which are subject to the imposition of this tax.

From a broader viewpoint, it is clear that allowing this tax to stand would lead to enactment of similar legislation in other States where multi-State generating facilities exist or are to be built.

Mr. Chairman, I will urge the Finance Committee to take action in this area in the immediate future in order to prohibit the taxation on the generation of electricity which finds its way into interstate commerce.

Thank you, Mr. Chairman.

Senator GRAVEL. I thank you.

Our first witness is——

Senator FANNIN. Mr. Chairman, pardon me. I would appreciate a statement being placed in the record from Senator Goldwater of Arizona.

Senator GRAVEL. We are happy to have it and it will be placed in the record.

[The prepared statement of Senator Goldwater follows:]

STATEMENT OF SENATOR BARRY GOLDWATER OF ARIZONA

UPHOLDING THE COMMERCE CLAUSE

Mr. Chairman, it is a pleasure for me to join with my colleague from Arizona, Senator Fannin, in sponsoring legislation that will uphold one of the basic doctrines of the Constitution which binds our 50 States into one nation. Our bill will reaffirm that the Commerce Clause of the United States Constitution is a restraint on the power of one State to hinder or discriminate against commerce moving into one or more of the other States.

To be specific, the bill will make it clear that no State has the right to tax the transmission of electricity generated in that State, but transmitted to and sold in another State. This is to halt the possible spread of laws such as the one enacted by New Mexico last year which creates a new electrical energy tax imposed on electricity generated in New Mexico and consumed in Arizona, California, Colorado and Texas. New Mexico utilities which sell power within New Mexico are in effect exempt from the tax because the law says that the electrical energy tax of such a utility shall be credited against the gross receipts tax otherwise due New Mexico. The energy tax wipes out the gross receipts tax for these in-State companies.

From this, no one can contend that the law is not discriminatory against power transmitted across State lines by out-of-State companies. Invariably, every press report announcing passage of the New Mexico law explained that in essence, out-of-State consumers would pay the tax. To make the law even more discriminatory against consumers in other States, it is tied to a companion bill that makes $1.3 million available to help reduce the utility bills of New Mexicans who are receiving welfare or other public assistance payments. In other words, Arizona citizens and the citizens of other States are to help foot the electricity bills of New Mexico residents.

Mr. Chairman, this is sufficient background to be aware that the New Mexico law and any that may follow in its pattern are a violation of the Constitutional doctrine of promoting the free flow of goods, services and business throughout the several States. That it was one of the first principles of the Constitution to protect commerce from State interferences with trade is beyond any question.

One of the first decisions Chief Justice Marshall ever wrote was to strike down a State law that had taxed the privilege of doing business in the State by companies outside the State. If it can tax that privilege, Marshall said, in the landmark case of *Gibbons* v. *Ogden*, it can exclude such companies altogether and this would nullify the whole purpose of the Founding Fathers to promote commerce among the States.

As Daniel Webster argued before the Supreme Court in this case, the prevailing motive of the Commerce Clause was to rescue commerce "from the embarrassing and destructive consequences, resulting from the legislation of so many different States." This argument was again accepted by Chief Justice Marshall in the case of *Brown* v. *Maryland*, decided 3 years later, which held a State tax on importers void as

an invalid regulation of foreign commerce. Then in 1873, the concept was applied to interstate commerce in the famous case of the *State Freight Tax*. This case squarely held that States may not tax property in transit in interstate commerce.

Applying the rule of Constitutional law clearly laid down by these cases, it is obvious that the New Mexico law conflicts with the Interstate Commerce Clause. The New Mexico energy tax places an extra burden on interstate commerce power transmitted outside of New Mexico that is not borne by intrastate commerce. The intrastate consumer enjoys a tax credit not granted to out-of-State consumers.

Mr. Chairman, the New Mexico law is directly aimed at electricity consumed outside the State. It will increase the energy bills of Arizona consumers by more than $3 million a year. It is flagrantly discriminatory against out-of-State consumers and against a product in interstate commerce. I urge that you approve our legislation and thereby reaffirm one of the primary, original aims of the Founding Fathers to promote commerce.

Senator GRAVEL. Our first witness is Henry Sargent, Jr., vice president of the Arizona Public Service Co., Phoenix, Ariz.

Do you have a statement for the record?

If you wish, you may summarize—however you feel more comfortable in making your presentation. Please sit down and feel at home.

STATEMENT OF HENRY B. SARGENT, JR., VICE PRESIDENT, ARIZONA PUBLIC SERVICE COMPANY, PHOENIX, ARIZ.

Mr. SARGENT. Thank you very much. I have a long statement I would like to file for the record and I have a shorter statement which is a condensation of that, if that is all right.

Senator GRAVEL. That shows great wisdom and understanding of the committee. [Laughter.]

You are off to a good start.

Mr. SARGENT. Thank you.

Mr. Chairman and members of the committee, my name is Henry B. Sargent, Jr., vice president for Finance and Treasurer of the Arizona Public Service Co., whose corporate headquarters is located in Phoenix Ariz.

We are the operating agent for the Four Corners Project near Farmington, N. Mex. The total generating capacity of the Four Corners Power Plant is 2,085,000 kilowatts. Almost 91 percent of the electricity generated at this power plant is exported from New Mexico to the States of Arizona, Texas and California.

Two of the participants in this plant are the Salt River Project and Tucson Gas & Electric Company. Collectively, together, we provided electrical service to 729,800 customers throughout the State of Arizona during 1975.

It is on behalf of these customers that I appear before you in support of the provisions contained in S. 1957, which would prohibit a State from imposing a tax on electricity which is generated within that State but which is moved in interstate commerce and consumed outside that State.

Many of you are aware that the State of New Mexico recently enacted an electrical generation tax. The amount of the tax is four-tenths of a mill per kilowatt-hour of electricity generated.

The practical effect of the legislation is to tax all electricity generated in that State which moves in interstate commerce and is consumed without the State, and to exempt from the generating tax the electricity generated and consumed within the State.

In the case of the Four Corners Power Plant, the estimated effect of this tax is to increase the cost of electricity exported from New Mexico by nearly $5 million in 1976.

Energy costs for customers of the three Arizona companies involved in Four Corners will increase approximately $3 million annually because of the generation tax levied by the State of New Mexico.

The State of Arizona has filed an action against the State of New Mexico in the U.S. Supreme Court asking the Court to assume original jurisdiction in this matter. The Court has yet to rule. I have attached a copy of this to my statement and would hope it will be placed in the record.

Five of the six participants in the Four Corners project have filed in the State District Court in Santa Fe, N. Mex. This Court has held initial hearings in the matter, but this case will take several years to reach a final determination in the U.S. Supreme Court.

I have also attached a copy of this filing, Exhibit B,* to my statement.

Mr. SARGENT. The tax has caused a great deal of concern in Arizona and has received much attention in the State legislature and in the press.

If the New Mexico tax is allowed to stand, I think it would be safe to guess that the Arizona Legislature at some point in the future will retaliate by placing a tax on electrical energy exported from Arizona.

I do not know what other southwestern States that are presently affected might do, but this tax has also caused considerable concern among energy users in California and Texas.

As most of us are now aware, electricity is no longer a luxury anywhere in the country, but is a necessity. The economy of the entire Nation is dependent on a dependable and sufficient supply of energy at the lowest reasonable cost.

In order to provide adequate supplies of energy at reasonable cost a significant trend among utilities in the Southwest has been to develop large, joint venture plants that serve customers in several States.

These multistate plants provide major economies of scale, but more important they are an efficient way of making maximum use of the limited number of plantsites that are available in our area of the country that have adequate water supplies and nearby fuel resources.

Our Four Corners Power Plant is just one example. Its largest units are owned jointly by six utilities, that provide energy to four States on a regular basis, that is, New Mexico, Texas, Arizona and California, and to two other States in times of emergency, Utah and Nevada.

Another example is the Navajo plant in Page, Arizona. It is also owned by six utility participants that provide energy to three States; in this case, Arizona, California and Nevada.

Still another example is the Mohave plant along the Colorado River in eastern Nevada. Four utilities participate in that project, providing energy to California, Arizona, and Nevada. The coal to fuel the Mohave plant is piped from northern Arizona to Nevada by slurry line.

More projects of this type are in advanced stages of planning in the Southwest.

*See page 27.

The Palo Verde Nuclear Power Plant in central Arizona will have a capacity of more than 3 million kilowatts. Its owners include six utilities that provide energy to customers in Arizona, California, New Mexico, and Texas.

Planning is nearly complete for the Kaiparowits coal-fired power plant in southern Utah which will have a capacity of more than 3 million kilowatts.

The three participants in Kaiparowits will supply energy from that plant to customers in Arizona and California.

This list of examples should make it clear that the opportunity exists for nearly every State in the Southwest to retaliate against taxes of the kind imposed by the State of New Mexico on electrical generation.

If retaliation were carried to an extreme it could become impossible for the electric industry to overcome the many barriers that would confront joint ventures in energy development.

Energy producers in the Southwest could be forced to step backward in time by returning to a system of small local generating plants that would in many cases be required to burn expensive imported oil as powerplant fuel.

We believe that taxes such as the New Mexico generating tax are not in the public interest and should be prohibited.

Mr. Chairman and members of the committee, on behalf of the customers of Arizona Public Service Co., Salt River project and Tucson Gas and Electric Co., we respectfully urge favorable and quick consideration of S. 1957.

I have also attached to my statement a copy of the New Mexico statutes, Exhibit C,* which you might wish to place in the record.

Senator GRAVEL. One question in my mind—and I am sure Senator Fannin will ask some questions—is the bone of contention the fact that they don't tax themselves the way they are taxing others who have to purchase the power.

If they taxed themselves the same way on the power they consume, would you still have opposition to this tax?

Mr. SARGENT. No. Our bone of contention is that it is a tax on power which is exported from the State and is paid for by customers in Arizona but is not paid for by people in New Mexico.

Senator GRAVEL. So, if they chose to tax uniformly, nobody would have a gripe?

Mr. SARGENT. Well, naturally, we wouldn't like it, but we wouldn't be here today.

Senator GRAVEL. Other than the taxpayers.

Mr. SARGENT. That is right.

Senator GRAVEL. I think that answers the question. What caused me to think of it is if somebody is selling crude oil to a generator for electricity outside the State, rather than electrical generation they could tax the crude oil if it came from in the State to an exhorbitant degree and that would be passed on through and have the same discriminatory facet to it.

Mr. SARGENT. Certainly.

Senator GRAVEL. In your mind that would similarly be illegal.

Mr. SARGENT. Yes, sir.

Senator GRAVEL. Supposing a State—take my own State. Supposing Alaska put a tax on exported oil, an exhorbitant tax on it.

*See page 38.

Would that fall in the same category?

Mr. SARGENT. We certainly wouldn't like to see any State pass a tax on natural gas, electricity, or whatever it might be, that apply only to those that were exported from the State.

If it applied to people within the State of Alaska or Arizona or wherever, I don't think there would be any objection to it.

Senator GRAVEL. You have answered my questions.

Thank you.

Senator Fannin?

Senator FANNIN. Yes, thank you.

In order to clarify the manner in which the tax applies, isn't it true, Mr. Sargent, that the tax, as far as New Mexico is concerned, is subject to rebate?

Mr. SARGENT. Yes, sir.

Senator FANNIN. So, the taxes are charged; as far as you know, it is all rebated in any event?

Mr. SARGENT. Let me put it this way: The tax is being assessed right now. The companies are not paying the tax but have filed suit in the State of New Mexico in the District Court so while we are having to charge the tax on our books, we are accruing the liability for that tax we are not yet paying in cash.

Senator FANNIN. What I am talking about is from the standpoint of the taxpayer—I mean, the people in New Mexico—the consumers in New Mexico. They pay the tax and they get a refund; isn't that correct?

Mr. SARGENT. Oh, yes. They have a gross receipts or a sales tax on sale of electricity within the State of New Mexico. So does Arizona.

New Mexico provides that the companies that do business in the State of New Mexico selling to customers there can take as a credit against the New Mexico gross receipts tax the amount paid in the New Mexico generation tax.

The net effect is they don't pay the New Mexico generating tax.

Senator FANNIN. This procedure is not available, of course, to the Arizona users or people outside the State of New Mexico?

Mr. SARGENT. That is correct. It is not.

Senator FANNIN. I just wanted to clarify that.

Senator GRAVEL. That is a very important clarification, too.

Senator FANNIN. You state, in your testimony, that enactment of the electrical energy tax could lead to the return to smaller generating facilities, as opposed to larger, more cost-efficient multi-State generating facilities.

Could you elaborate on the economic consequences that such a result would have on the consumers?

Mr. SARGENT. Yes.

If this were carried to extreme, Senator Fannin, and we are not able to build these large powerplants of, say, 800 megawatt units, which is the size roughly of the Four Corners units, we would instead have to build smaller units located closer to load centers, Phoenix or Tucson or other cities in the Southwest.

This being so far from the coal mines, it would mean we would have to burn oil instead of coal, probably, and so there really are

two economic consequences: One is that the smaller units themselves are much more expensive to build than a big unit per kilowatt of installed capacity.

A big 800 megawatt unit in 1980, we estimate would cost around $600 per kilowatt to install whereas a small 100 megawatt unit such as the ones we would probably be building around our load centers would cost—I said that backwards. The big units would cost about $450 per kilowatt; the smaller units would cost about $600 per kilowatt.

So that is an increase of about one-third. But, if we had to burn oil, it would cost us about ten times as much as coal that we burn at Four Corners. So, that would have a tremendous impact on consumers if we had to go that route.

Senator FANNIN. It has been estimated that the average annual additional cost to individual Arizona consumers would be in the range of $2 or $3 a year.

However, additional costs to institutional facilities would be significantly higher. Could you comment on that?

Mr. SARGENT. Yes, while the residential ratepayer would pay about $2.40 a year in our case for the New Mexico tax, we have some much bigger customers to which this is a substantial amount.

Our largest customer is a copper company and they pay us over $100,000 a year on account of the New Mexico tax. Arizona State University, which is one of our largest commercial customers, is paying us about $20,000 a year on this tax; and the average shopping center-type of department store or office building pays us between $2,000 and $3,000 per year.

Senator FANNIN. So, the schools would be vitally affected, hospitals, public facilities and all the different institutional operations would be vitally affected?

Mr. SARGENT. They certainly would.

Senator FANNIN. Your testimony indicates other States may retaliate against New Mexico by enacting new taxes on not only electricity but on the sources of generating power such as coal.

Would not such a series of events lead to a greater uncertainty for the utilities and the consumers, the customers they serve, thereby inhibiting and further delaying the construction of necessary new facilities?

Mr. SARGENT. It certainly would, yes.

Senator FANNIN. While the present electrical energy tax rate of four-tenths of 1 percent will yield a relatively small sum of $5 million, is there any reason to believe that this tax rate would not be increased in the future if this tax is allowed to stand?

Mr. SARGENT. That is the thing that worries us most of all, Senator Fannin. This tax could increase to enormous proportions in the future.

If it is finally allowed to stand and the States find they can assess ratepayers in other States and not assess their own customers and voters within that State, we think that this kind of thing could get very popular and really could be catastrophic toward development in the Southwest.

Senator FANNIN. I think it has dire consequences, even if you just take into consideration our educational institutions, both the elementary and secondary and higher institutional authorities.

As you know, Congress regulates interstate commerce. Do joint ventures by utilities for more than one State, in addition to the fact that much of the electricity is immediately transmitted across State lines, cause you to characterize these operations as interstate commerce?

Mr. SARGENT. Yes, sir.

Senator FANNIN. Well, thank you very much for your testimony.

Senator GRAVEL. Thank you, sir.

[The prepared statement of Mr. Sargent with attachments follows. Oral testimony continues on p. 31.]

STATEMENT BY HENRY B. SARGENT, JR., VICE PRESIDENT, ARIZONA PUBLIC SERVICE COMPANY

Mr. Chairman and members of the committee, my name is Henry B. Sargent, Jr., vice president for Finance and treasurer of Arizona Public Service Co., whose corporate headquarters is located in Phoenix, Arizona. We are the operating agent for the Four Corners Project near Farmington, N. Mex. The total generating capacity of the Four Corners Power Plant is 2,085,000 kilowatts. Almost 91 percent of the electricity generated at this powerplant is exported from New Mexico to the States of Arizona, Texas and California.

Two of the participants in this plant are the Salt River Project and Tucson Gas and Electric Co. Collectively we provided electrical service to 729,800 customers throughout the State of Arizona during 1975.

It is on behalf of these customers that I appear before you in support of the provisions contained in S. 1957, which would prohibit a State from imposing a tax on electricity which is generated within that State but which is moved in interstate commerce and consumed outside that State.

Many of you are aware that the State of New Mexico recently enacted an electrical generation tax. The amount of the tax is four-tenths of a mill per kilowatt-hour of electricity generated. The practical effect of the legislation is to tax all electricity generated in that State which moves in interstate commerce and is consumed without the State, and to exempt from the generating tax most, if not all, of the electricity generated and consumed within the State.

In the case of the Four Corners Power Plant, the estimated effect of this tax is to increase the cost of the electricity exported from New Mexico by nearly $5 million in 1976.

Energy costs for customers of the three Arizona companies involved in Four Corners are projected to increase approximately $3 million annually because of the generation tax levied by the State of New Mexico.

The State of Arizona has filed an action against the State of New Mexico in the U.S. Supreme Court asking the Court to assume original jurisdiction in this matter, a copy of which is attached as exhibit A. The Court has yet to rule. Five of the six participants in the Four Corners Project (Public Service Company of New Mexico is not a party to the suit) have filed in the State District Court in Santa Fe, New Mexico. A copy of this filing is also attached as Exhibit B. This Court has held initial hearings in the matter, but this case will take several years to reach a final determination in the U.S. Supreme Court.

The New Mexico Legislature had for a number of years attempted to enact some form of a generation tax. The proposed rate of tax has varied from four-tenths of a mill to 4 mills per kilowatt-hour. In 1975, they achieved success and today the State of New Mexico, pursuant to Chapter 72, Article 34 NMSA, levies a tax of four-tenths of a mill per kilowatt-hour on all electricity generated in that State (see Exhibit C).

In addition, New Mexico collects from the seller a 4 percent gross receipts tax on all sales of electricity to that State's consumers (see Exhibit D). In order to relieve the New Mexico customer of the added cost of the generation tax each utility is allowed a credit against the 4 percent gross receipts tax in an amount equal to that paid on the generation tax. Section 72-16A-16.1 NMSA reads in part as follows:

> B. On electricity generated inside this State and consumed in this State which was subject to the electrical energy tax, the amount of such tax paid *may be credited* against the gross receipts tax due this state. (Emphasis added.) (See Exhibit E.)

Utilities who have no retail sales in New Mexico, which is the situation in the case of Arizona Public Service, Salt River Project, and Tucson Gas and Electric, are unable to take credit for generation taxes paid. The practical effect of this then is that electric customers in New Mexico pay no generation tax but all electric customers outside the State pay it.

You will note in reading Chapter 72, Article 34 NMSA that the statute specifically provides for the subject tax on generation to be temporary and to expire in 1984. While the present statute may provide for this tax to self-destruct, as a practicable matter we do no expect this to happen because of long-range expenditure commitments that were enacted and signed into law as companion legislation.

Chapter 145 Laws of 1975 of New Mexico appropriates an amount not to exceed $32 million from the revenues derived from proceeds of the generation tax for the construction or improvement of New Mexico roads 44 and 371, U.S. Highway 666 and roads designated as N-36 and RD-3005 within the State of New Mexico.

Section 13-20-1, et seq. NMSA provides for an appropriation, pursuant to the New Mexico Utility Supplement Act to be used as follows:

> 13-20-2. Legislative intent.—It is the intent of the Legislature that the Utility Supplement Act (13-20-1 to 13-20-9) be used to assist recipients of Federal supplemental security income benefits and recipients of aid to families with dependent children in meeting increased costs for *gas and electrical utilities to the maximum extent possible*. The appropriation made in the Utility Supplement Act shall be used to generate those Federal funds which may be available. (Emphasis added.)

In fact, without the revenues provided by the Electrical Energy Tax Act, the Utility Supplement Act becomes inoperative, as we can see by reading Section 13-20-9 NMSA:

> 13-20-9. No payment during injunction.—If the State should be sued by a party seeking to prohibit the collection of the tax provided for in the Electrical Energy Tax Act (72-34-1 to 72-34-6), no payments shall be made under the Utility Supplement Act (13-20-1 to 13-20-9) during the pendency of the suit and no payments shall be made if the Electrical Energy Tax Act is ultimately held invalid in any suit.

The tax has caused a great deal of concern in Arizona and has received much attention in the State Legislature and in the press. If the New Mexico tax is allowed to stand, I think it would be safe to guess that the Arizona Legislature at some point in the future will retaliate by placing a tax on electrical energy exported from Arizona. I do not know what other southwestern States that are presently affected might do, but this tax has also caused considerable concern among energy users in California and Texas.

As most of us are now aware, electricity is no longer a luxury anywhere in the country, but is a necessity. The economy of the entire nation is dependent on a dependable and sufficient supply of energy at the lowest reasonable cost.

In order to provide adequate supplies of energy at reasonable cost a significant trend among utilities in the Southwest has been to develop large, joint venture plants that serve customers in several States. These multistate plants provide major economies of scale, but more important they are an efficient way of making maximum use of the limited number of plantsites that are available in our area of the country that we have adequate water supplies and nearby fuel resources. Our Four Corners Power Plant is just one example. Its largest units are owned jointly by six utilities that provide energy to four states on a regular basis (New Mexico, Texas, Arizona and California) and to two other states in times of emergency (Utah and Nevada). Another example is the Navajo plant in Page, Arizona. It is also owned by six utility participants that provide energy to three states, in this case, Arizona, California and Nevada. Still another example is the Mohave plant along the Colorado River in Eastern Nevada. Four utilities participate in that project, providing energy to California, Arizona and Nevada. The coal to fuel the Mohave plant is piped from northern Arizona by slurry line to Nevada.

More projects of this type are in advanced stages of planning in the Southwest.

The Palo Verde Nuclear Power Plant in central Arizona will have a capacity of more than 3 million kilowatts. Its owners include six utilities that provide energy to customers in Arizona, California, New Mexico and Texas. Planning is nearly complete for the Kaiparowits coal-fired powerplant in southern Utah which will have a capacity of more than 3, million kilowatts. The three participants in Kaiparowits will supply energy from that plant to customers in Arizona and California.

This list of examples should make it clear that the opportunity exists for nearly every State in the Southwest to retaliate against taxes of the kind imposed by the State of New Mexico on electrical generation. If retaliation were carried to an extreme it could become impossible for the electric industry to overcome the many barriers

that would confront joint ventures in energy development. Energy producers in the Southwest could be forced to step backward in time by returning to a system of small local generating plants that would in many cases be required to burn expensive imported oil as powerplant fuel.

We believe that taxes such as the New Mexico Generating Tax are not in the public interest and should be prohibited.

Mr. Chairman and members of the Committee, on behalf of the customers of Arizona Public Service Company, Salt River Project and Tucson Gas and Electric Company, we respectfully urge favorable and quick consideration of S. 1957.

ATTACHMENTS

EXHIBIT A

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1975

Arizona, Plaintiff, v. *New Mexico*, Defendant.

Motion For Leave To File Complaint And Complaint.

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CONSTITUTIONAL PROVISIONS

United States Constitution, Article III, Section 2:

"The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority;—to all Cases affecting Ambassadors, other public Ministers and Consuls;—to all cases of admiralty and maritime Jurisdiction,—to Controversies to which the United States shall be a Party;—to Controversies between two or more States;—between a State and Citizens of another State;—between Citizens of different States;—between Citizens of the same State claiming Lands under Grants of different States, and between a State, or the Citizens thereof, and foreign States, Citizens or Subjects.

"In all Cases affecting Ambassadors, other public Ministers and Consuls, and those in which a State shall be Party, the Supreme Court shall have original Jurisdiction. In all the other Cases before mentioned, the Supreme Court shall have appellate Jurisdiction, both as to Law and Fact, with such Exceptions, and under such Regulations as the Congress shall make."

United States Constitution, Article IV, Section 2:

"The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States."

United States Constitution, Fourteenth Amendment, Section 1:

"All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

United States Constitution, Article I, Section 8:

"The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."

FEDERAL STATUTES

28 U.S.C. Section 1251 (a) (1) (1966).
Federal Power Act, 16 U.S.C. Section 824 (a) (1935).

STATE STATUTES

The New Mexico Statute here in issue is reproduced in full on page 26.

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1975

Arizona, Plaintiff, v. *New Mexico*, Defendant.

Motion For Leave To File Complaint

Pursuant to Rule 9 of the Rules of the Supreme Court, the State of Arizona, by its Attorney General, asks leave of this Court to file its Complaint, submitted herewith, against the State of New Mexico.

Bruce E. Babbitt, 159 State Capitol, Phoenix, Arizona, Arizona Attorney General

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IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1975

Arizona, Plaintiff, v. *New Mexico*, Defendant.

COMPLAINT

The State of Arizona alleges the following causes of action against the State of New Mexico.

FIRST CAUSE OF ACTION

I.

The original and exclusive jurisdiction of this Court is invoked under the authority of Article III, Section 2, Paragraphs 1 and 2 of the Constitution of the United States and 28 U.S.C. Section 1251 (a) (1) (1966).

II.

Plaintiff State of Arizona and defendant State of New Mexico are sovereign States of the United States.

III.

Plaintiff herein has no plain, speedy, or adequate remedy at law and has no remedy whatsoever in any other court.

IV.

Plaintiff brings this First Cause of Action in its proprietary capacity and in that capacity will sustain substantial monetary damage as a result of the unconstitutional acts of defendant.

V.

Chapter 263 of New Mexico Laws of 1975, which became effective July 1, 1975, purports to impose a privilege tax on the generation of electrical energy within New Mexico. A copy of that Act (hereinafter referred to as the "Electrical Energy Tax" or the "Act") is attached hereto as Exhibit "A" and is incorporated herein as though set forth in detail.

> Section 3.A of the Act provides: For the privilege of generating electricity in this State for the purpose of sale, whether the sale takes place in this State or outside this State, there is imposed on any person generating electricity a temporary tax, applicable until July 1, 1984, of four-tenths of one mill ($.0004) on each net kilowatt hour of electricity generated in New Mexico.
>
> Section 9 of the Act provides:
>
> A. If on electricity generated outside this State and consumed in this State, an electrical energy tax or similar tax on such generation has been levied by another State or political subdivisions thereof, the amount of such tax paid may be credited against the gross receipts tax due this State.
>
> B. On electricity generated inside this State and consumed in this State which was subject to the electrical energy tax, the amount of such tax paid may be credited against the gross receipts tax due this State.
>
> C. The credit under Subsections A or B of this section shall be assigned to the person selling the electricity for consumption in New Mexico on which New Mexico gross receipts tax is due, and the assignee shall reimburse the assignor for the credit.

Section 9.B of the Act thus provides for a credit against the New Mexico Gross Receipts Tax for the Electrical Energy Tax paid upon electricity generated in New Mexico and consumed within New Mexico. No credit against the New Mexico Gross Receipts Tax is available with respect to the Electrical Energy Tax imposed upon electricity generated in New Mexico but consumed outside New Mexico. The interrelationship of Section 3.A and Section 9 of the Act in practical operation and effect intentionally shifts the incidence of the Electrical Energy Tax from the generation of electrical energy to the interstate transmission of electrical energy outside New Mexico.

VI.

Three Arizona entities, Arizona Public Service Company, Tucson Gas & Electric Company, and Salt River Project, own as tenants in common interests in electrical generating facilities in New Mexico. Two of the three Arizona entities are investor-owned public service corporations; the third, Salt River Project, is a political subdivision of the plaintiff. Electrical energy is generated at such facilities in response to consumer demands in Arizona, and this energy is instantaneously transmitted in interstate commerce to Arizona consumers. The generation of electrical energy in response to consumer demands in Arizona is inseparable from its interstate transmission to Arizona and constitutes interstate commerce.

VII.

Plaintiff consumes and pays for large quantities of electrical energy generated in New Mexico. The Electrical Energy Tax applies to all such electrical energy and will be paid by plaintiff through charges for energy consumed by it. Therefore, the incidence and burden of the Electrical Energy Tax falls upon plaintiff.

VIII.

Many political subdivisions of plaintiff, including community college districts, counties, cities and school districts, consume and pay for large quantities of electrical energy generated in New Mexico. The Electrical Energy Tax applies to all such electrical energy and will be paid by such political subdivisions through charges for energy consumed by them. Plaintiff, through appropriation and revenue sharing, makes state funds directly available to its political subdivisions for the purpose of assisting in defraying the costs of local government, including payment of charges for energy consumed by them. Therefore, the incidence and burden of the Electrical Energy Tax falls upon plaintiff.

IX.

The Electrical Energy Tax constitutes an unreasonable discrimination against and an unconstitutional burden on interstate commerce.

SECOND CAUSE OF ACTION

I.

Plaintiff realleges, as though set forth in full, Paragraphs I, II, III, V, VI and IX of the First Cause of Action.

II.

Plaintiff brings this Second Cause of Action in its *parens patriae* or quasi-sovereign capacity.

III.

The vast majority of the citizens of Arizona consume and pay for electrical energy generated in New Mexico. The Electrical Energy Tax applies to all such electrical energy and will be paid by Arizona consumers through charges for energy consumed by them. Therefore, the incidence and burden of the Electrical Energy Tax falls upon Arizona citizens.

IV.

The Act discriminates, and was intended to discriminate, against the citizens of Arizona, by placing upon them the substantial burdens of the Electrical Energy Tax, a burden not borne by the citizens of New Mexico by reason of the credit provisions of Section 9 of the Act.

V.

The Act denies to Arizona citizens due process of law in violation of the Fourteenth Amendment to the United States Constitution.

VI.

The Act denies to citizens of Arizona the equal protection of the law in violation of the Fourteenth Amendment to the United States Constitution.

VII.

The Act abridges the privileges and immunities of citizens of Arizona guaranteed to them by Article IV, Section 2 of the United States Constitution.

Wherefore Plaintiff Prays That: 1. The Court declare that the Act constitutes an unconstitutional discrimination against and burden upon interstate commerce.

2. The Court declare that the Act denies to Arizona citizens due process of law in violation of the Fourteenth Amendment to the United States Constitution.

3. The Court declare that the Act denies to citizens of Arizona equal protection of the law in violation of the Fourteenth Amendment to the United States Constitution.

4. The Court declare that the Act abridges the privileges and immunities of citizens of Arizona guaranteed to them by Article IV, Section 2 of the United States Constitution.

5. The Court restrain and enjoin the State of New Mexico from assessing, levying or collecting the tax imposed by the Act.

6. The Court award to plaintiff and against defendant plaintiff's costs expended and incurred in this suit.

7. The Court grant plaintiff such other and further relief as the Court may deem justified.

Bruce E. Babbitt, 159 State Capitol, Phoenix, Ariz., Arizona Attorney General.

EXHIBIT "A" Chapter 263

An Act relating to taxation: imposing a tax on the generation of electricity; amending sections 45-4-28 and 72-13-24 NMSA 1953 (being laws 1939, Chapter 47, Section 28 and laws 1965, Chapter 248, Section 12, as amended); enacting a new section 72-16A-16.1 NMSA 1953.

Be it enacted by the Legislature of the State of New Mexico:

Section 1. Short Title—Sections 1 through 6 of this act may be cited as the "Electrical Energy Tax Act".

Section 2. Definitions.—As used in the Electrical Energy Tax Act:

A. "bureau" means the New Mexico bureau of revenue;

B. "generation" includes manufacture and production;

C. "electricity" includes electrical energy and electrical power;

D. "person" means any individual, estate, trust, receiver, cooperative association, electric cooperative, club, corporation, company, firm, partnership, joint venture, syndicate, association, irrigation district, electrical irrigation district and any utility owned or operated by a county or municipality, and also means to the extent permitted by law, any Federal, State or other governmental unit or subdivision or an agency, department or instrumentality; and

E. "sale" means selling or transferring to any person for consumption, use or resale and includes barter and exchange.

Section 3. Imposition of Tax—Rate—Denomination as Electrical Energy Tax.

A. For the privilege of generating electricity in this State for the purpose of sale, whether the sale takes place in this State or outside this State, there is imposed on any person generating electricity a temporary tax, applicable until July 1, 1984, of four-tenths of one mill ($.0004) on each net kilowatt hour of electricity generated in New Mexico.

B. The tax imposed by this section shall be referred to as the "electrical energy tax."

Section 4. Measurement and Recording of Kilowatt Hours of Electricity.—Persons subject to the imposition of the electric energy tax shall maintain accurate measuring devices and records to measure and record the daily and cumulative monthly and yearly totals of kilowatt hours of electricity generated or distributed in this State.

Section 5. Reports—Remittances.—Every person subject to the imposition of the electrical energy tax shall file a return on forms provided by and with the information required by the bureau and shall pay the tax due on or before the 25th day of the 2nd month following the month in which the taxable event occurs.

Section 6. Relief From Other Taxes.—Unless otherwise specified by statute the imposition of the electrical energy tax shall not act to relieve any person or activity from any other tax levied by the State of New Mexico or its political subdivisions.

Section 7. Section 45-4-28 NMSA 1953 (being Laws 1939, Chapter 47, Section 28, as amended) is amended to read:

"45-4-28. Taxation.—Cooperative and foreign corporations, transacting business in this State pursuant to the provisions of Sections 45-4-1 through 45-4-32 NMSA 1953 shall pay annually, on or before July 1, to the state corporation commission, a tax of ten dollars ($10.00) for each 100 persons or fraction thereof to whom electricity is supplied within this state which tax shall be in lieu of all other taxes except those provided in the Gross Receipts and Compensating Tax Act, and the Electrical Energy Tax Act; provided, however, that in the event a contract has been entered into by a rural electric cooperative and a power consumer prior to February 1, 1961, and such contract does not contain an escalator clause providing for an increase for added tax liability on the cooperative, then the sale to such power consumer shall be exempt until the expiration, extension or renewal of the contract."

Section 8. Section 72-12-24 NMSA 1953 (being Laws 1965, Chapter 248, Section 12, as amended) is amended to read:

"72-13-24. Receipts—Disbursements—Distribution.

A. All money received by the bureau shall be deposited with the State treasurer before the close of the next succeeding business day after receipt of the money.

B. Money received or disbursed by the bureau shall be accounted for by the commissioner as required by law or regulation of the director of the department of finance and administration.

C. Disbursements for tax credits, refunds and the payment of interest shall be made by the department of finance and administration upon request and certification of their appropriateness by the commissioner or his delegate. The State treasurer shall create a suspense fund for the purpose of making the disbursements authorized by the Tax Administration Act. All revenues collected pursuant to the provisions of Sections 72-15-1 through 72-15-37 NMSA 1953, the Income Tax Act, the Withholding Tax Act, the Gross Receipts and Compensating Tax Act, the Resources Excise Tax Act, the Liquor Excise Tax Act and the Electrical Energy Tax Act shall be credited to this suspense fund and are appropriated for the purpose of making disbursements for tax credits, refunds and the payment of interest.

D. On the last day of each month, any money remaining in the suspense fund after the necessary disbursements have been made shall be identified by tax source and transferred from the suspense fund, one-half of the receipts attributable to the electrical energy tax shall be transferred to the "electrical energy fund", hereby created, and the remainder to the state general fund, except that before the remaining money is transferred to the general fund, an amount equal to 1 percent of the taxable gross receipts reported for the month of deposit:

(1) for each municipality shall be distributed to each municipality: and (2) by taxpayers who have business locations on an Indian reservation or pueblo grant in an area which is contiguous to a municipality and in which the municipality performs services pursuant to a contract between the municipality and the Indian tribe or Indian pueblo shall be distributed to the municipality if:

(a) the contract describes the area in which the municipality is required to perform services and requires the municipality to perform services that are substantially the same as the services the municipality performs for itself; and (b) the governing body of the municipality has submitted a copy of the contract to the commissioner of revenue.

E. Disbursements to cover expenditures of the bureau shall be made only upon approval of the commissioner or his delegate.

F. Miscellaneous receipts from charges made by the bureau to defray expenses pursuant to the provisions of Section 72-13-23 and 72-13-39 NMSA 1953 and similar charges are appropriated to the bureau for its use."

Section 9. A new Section 72-16A-16.1 NMSA 1953 is enacted to read:

"72-16A-16.1. Credit—Gross Receipts Tax.

A. If on electricity generated outside this State and consumed in this State, an electrical energy tax or similar tax on such generation has been levied by another State or political subdivisions thereof, the amount of such tax paid may be credited against the gross receipts tax due this State.

B. On electricity generated inside this State and consumed in this State which was subject to the electrical energy tax, the amount of such tax paid may be credited against the gross receipts tax due this State.

C. The credit under subsections A or B of this section shall be assigned to the person selling the electricity for consumption in New Mexico on which New Mexico gross receipts tax is due, and the assignee shall reimburse the assignor for the credit."

Section 10. Legislative Intent.—It is the intent of the legislature that this entire 1975 act be considered not severable, and should any part hereof be declared unconstitutional, the entire Act should be declared void.

Section 11. Effective Date.—The effective date of the provisions of this Act is July 1, 1975.

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1975

Arizona, Plaintiff, v. *New Mexico*, Defendant

Brief In Support Of Motion For Leave To File Complaint

I

THIS COURT HAS ORIGINAL AND EXCLUSIVE JURISDICTION OF THIS CONTROVERSY

Plaintiff's Motion for Leave to File Complaint seeks to challenge the constitutionality of the Electrical Energy Tax Act (the "Act") enacted by the State of New Mexico as Chapter 263, New Mexico Laws of 1975, which purports to impose a tax on the privilege of generating electricity in New Mexico. This case should not present any significant factual issues; the central constitutional issues are clearly posed by the Act itself.

This controversy between the State of Arizona and the State of New Mexico is within the original and exclusive jurisdiction of this Court under Article III, Section 2, Paragraphs 1 and 2 of the Constitution of the United States and 28 U.S.C. Section 1251(a)(1).

The State of Arizona, in its proprietary capacity, is a major consumer of electrical energy generated in New Mexico. The tax sought to be imposed by New Mexico applies to such electrical energy and will be paid for by the State of Arizona through charges for energy consumed by it. Injury, therefore, will be done to the State of Arizona in its propietary capacity. *North Dakota* v. *Minnesota*, 263 U.S. 365 (1923). This interest is independent of the interests of its citizens. *Georgia* v. *Tennessee Copper Co.*, 206 U.S. 230 (1907). Further, potential injury to the educational institutions, as consumers, and as instrumentalities of the State of Arizona, is injury to the State itself. *Arkansas* v. *Texas*, 346 U.S. 368 (1953). Arizona has no forum other than this Court in which to assert its claim. *Illinois* v. *Milwaukee*, 406 U.S. 91 (1972).

The State of Arizona is also suing as *parens partriae* for and on behalf of its citizens who are consumers of electrical energy generated in New Mexico. The right of the State to bring such an action has been recognized by this Court. *Hawaii* v. *Standard Oil Co.*, 405 U.S. 251 (1972); *Georgia* v.*Pennsylvania Railroad Co.*, 324 U.S. 439 (1945). This is indeed an appropriate case for the State of Arizona to sue as *parens patriae*. The actions of the State of New Mexico threaten the very health, welfare, and comfort of the citizens of Arizona who consume electrical energy generated in New Mexico. *Pennsylvania* v. *West Virginia*, 262 U.S. 553 (1923). Thus, regardless of pecuniary interest, the State of Arizona has standing here to protect its citizens. *Kansas* v. *Colorado*, 206 U.S. 46 (1907).

STATEMENT OF THE CASE

The purpose of this litigation is to challenge the constitutionality of the Act, a copy of which is attached to Plaintiff's Complaint as Exhibit "A".

Section 3.A of the Act imposes a tax of four-tenths of a mill per net kilowatt hour of electricity generated within the State of New Mexico, ostensibly "for the privilege of generating electricity [in New Mexico] for the purpose of sale."

Section 9 of the Act grants complete relief from the tax, however, for all electricity generated *and consumed in New Mexico*. The exemption is achieved by adding to the New Mexico gross receipts tax (72-16A-16.1 NMSA 1953) a clause which exempts from the electrical generation tax (by means of a 100 percent credit against the gross receipts tax) "electricity generated inside this state and consumed in this state."

Other provisions of the Act establish the credit provision as the central and operational feature of the Act. Section 10 states that the Act is to be considered inseverable and "should any part hereof be declared unconstitutional, the entire Act should be declared void", thereby insuring that the citizens of New Mexico shall in no way bear any burden of the tax. The net operational effect of the Act is such that the entire burden of the tax is borne by citizens of States other than New Mexico.

The State of Arizona and its citizens are consumers of substantial amounts of electrical energy generated in New Mexico. Enormous amounts of electricity are generated at facilities located within New Mexico in response to demands for electricity in other States; such electricity is transmitted instantaneously to interstate markets over interstate transmission lines. The electrical systems of all entities owning generating facilities

in New Mexico are wholly or substantially interconnected, and the amount of energy generated in New Mexico at any time is determined by the total demands of electricity on the interconnected system at that time.

QUESTIONS PRESENTED

New Mexico has enacted an Electrical Energy Tax Act which taxes all electrical energy produced in that State and consumed outside New Mexico and which exempts from the tax (by means of a tax credit) any similarly produced electrical energy consumed within New Mexico. The questions presented are:

I. Whether the tax is an unconstitutional discrimination against or burden upon interstate commerce.

II. Whether the tax imposes a discriminatory burden on non-residents of New Mexico in violation of the Interstate Privileges and Immunities Clause or the Equal Protection Clause of the Fourteenth Amendment.

ARGUMENT

I. The Act is an Unconstitutional Discrimination Against and Burden Upon Interstate Commerce.

A. *The Act discriminates against interstate commerce.*

This Court, in determining the constitutionality of a State tax affecting interstate commerce, is concerned with the practical application of the tax in question. Regardless of how a tax may be denominated, labeled, or measured, the ultimate question is whether the tax in fact discriminates against interstate commerce or in favor of similarly placed local or intrastate business. *Halliburton Oil Well Cementing Co.* v. *Reily*, 373 U.S. 64 (1963); *Alaska* v. *Arctic Maid*, 366 U.S. 199 (1961); *Spector Motor Service, Inc.* v. *O'Connor*, 340 U.S. 602, 608 (1951). ("It is not a matter of labels.")

The Act purports to impose a privilege tax on the manufacture and production of electricity in New Mexico. Beneath the label, however, the Act in fact imposes a tax which falls exclusively on the interstate transmission of electrical energy for consumption outside the State of New Mexico. Section 3.A of the Act, which purports to impose the tax generally on all electricity generated, is followed by Section 9, which grants 100 percent credit against the New Mexico gross receipts tax for the electrical generation tax paid upon any electricity which is ultimately consumed in New Mexico.

In result, there is no dollars and cents tax liability for electricity generated and consumed in New Mexico; the apparent liability created by Section 3 is washed out by the credit provision of Section 9 for in-State consumption. The result is a "paper" tax erased by a "paper" credit upon all electricity generated and consumed in New Mexico.

However, for electricity generated in New Mexico and consumed outside the State, the credit provision is inoperative and the tax thereby becomes a true dollar liability at the point the electricity leaves New Mexico for consumption elsewhere. What purports to be a tax on privilege of *generating* electricity in New Mexico is in fact an unconstitutional tax imposed solely on the privilege of *transmitting* electricity in interstate commerce. *Spector Motor Service, Inc.* v. *O'Connor*, 340 U.S. 602 (1951).

Such complete discrimination, by artful separation of only that segment of the energy destined for out-of-State sale to bear the entire tax, is plainly unconstitutional. This Court has, in a variety of less egregious factual settings, held that States cannot single out interstate activities for special taxes that are not borne by similarly situated local activities. *Halliburton Oil Well Cementing Co.* v. *Reily*, 373 U.S. 64 (1963) (holding unconstitutional a Louisiana use tax that imposed different standards resulting in higher taxes on property manufactured out-of-State; *West Point Grocery Co.* v. *Opelike*, 354 U.S. 390 (1957) (invalidating municipal tax on wholesale grocers operating outside city on ground that effect was to discriminate against out-of-State wholesalers); *Memphis Steam Laundry Cleaner, Inc.* v. *Stone*, 342 U.S. 389 (1952) (voiding as violative of the Commerce Clause a Mississippi tax of $50 per out-of-State laundry truck as compared to $8 per truck within Mississippi), *Nippert* v. *Richmond*, 327 U.S. 416 (1946) (invalidating license tax on solicitors because of strong likelihood of discrimination against interstate commerce in favor of local business). *Cf. Alaska* v. *Arctic Maid*, 366 U.S. 199 (1961) (upholding a freezer ship tax upon finding that the tax did not discriminate in favor of local Alaska industry).

B. *The Act places an unconstitutional burden upon interstate commerce.*

Apart from its discriminatory effect, the Act, by directly taxing the flow of electrical energy in interstate commerce, places an impermissible burden on the flow of interstate commerce. In *Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 347 U.S. 157 (1954), the Court considered whether the Commerce Clause was infringed by a Texas tax

on the occupation of "gathering gas", measured by the volume of gas "taken", as applied to an interstate natural gas pipeline company taking gas for the purpose of immediate interstate transmission. While the tax applied equally to gas moving in interstate and intrastate commerce, the Court noted that the statute prohibited the shifting of the tax back to the producer (presumably with the same design as the credit provision in the present case), that the statute had an inseverability provision (analogous to the inseverability provision in the present case), and that, as in the present case, the incidence of the tax had been delayed beyond the step where production had ceased and transmission in interstate commerce had begun. Characterizing the statute as in reality a tax "on the exit of gas from the state", the Court noted that the gathering of the gas into transmission lines was so integrally tied to interstate commerce that if Texas could impose such a tax, the door would be opened for the recipient and intermediary states to levy a tax directly on the volume of the gas in the pipeline as the gas crossed their boundaries. "The net effect would be substantially to resurrect the customs barriers which the Commerce Clause was designed to eliminate." 347 U.S. at 170.

The generation and transmission of electricity in the southwestern United States in the year 1975 is inseparably a part of interstate commerce, to an extent not even conceived a few decades earlier. Electrical generating facilities throughout the southwestern states are now linked in a vast interstate grid of transmission and distribution lines. (Appendix "A", a map of the principal transmission lines on January 1, 1975 prepared by the Western Systems Coordinating Council, illustrates this fact.)

Markets demanding electrical energy are supplied from all generators on the interstate system without regard to State boundaries. Dispatchers control generation facilities throughout the interstate system to utilize the most efficient generating facilities and to minimize costs per kilowatt hour. Their decisions are made in response to demands placed on the total interstate system by all consumers without regard to state boundaries. Electricity is not generated in hope that demand will clear the available commodity from the market; rather it is generated solely in response to market demand and fluctuates on the interstate system from minute to minute each day throughout the year.

The principle of *Michigan-Wisconsin*, protecting an interstate gas transmission system from customs tariffs and the potential multiple burdens of state taxation, is even more valid and more urgently required in the present context. In the midst of an international energy crisis, with all its implications for the American economy, individual states cannot be allowed to step in and disrupt the regional and national flow of electrical energy by levying taxes directly on the volume flow of such energy.

Plaintiff does not contend that truly local activities of entities producing power cannot be taxed. New Mexico can and does levy an ad valorem property tax on the modern, complex generating facilities that are linked to the interstate system. New Mexico can and does levy privilege license taxes on domestic and foreign corporations such as the utilities that engage in business in New Mexico.

However, if New Mexico's power to tax is extended to a direct levy on the volume of electricity which instantaneously becomes part of a high voltage, interconnected system serving the entire southwest, the possibilities for multiple taxation and interference with a smoothly functioning interstate energy system are obvious and impermissible. Any tax measured by the amount of electricity flowing into the interstate system invites other States similarly to tax the volume of electricity crossing their borders or passing through transformers within their borders. The result would be an impermissible direct taxation of, and the imposition of multiple burdens on, the movement of electricity in the interstate system. *Evco* v. *Jones*, 409 U.S. 91 (1972) (distinguishing invalid New Mexico gross receipts tax upon out-of-State sales of finished product and permissible tax upon income derived from services performed within New Mexico).

Thus as the Court recognized in *Michigan-Wisconsin*, the direct taxation of the interstate transmission of energy measured by volume, in fact, provides a method of taxation that strikes directly at the flow of interstate commerce. The flow of energy in interstate commerce, prohibited from being so taxed, is far removed from the "localized alternative incidents" which the States have been permitted to tax. *Colonial Pipeline Co.* v. *Traigle*, 95 S.Ct. 1538, 1543 (1975); *Joseph* v. *Carter & Weekes Stevedoring Co.*, 330 U.S. 422 (1947) (tax upon a stevedoring business impermissible as direct interference of the loading of an interstate carrier); *Western Union Telegraph Co.* v. *Texas*, 105 U.S. 460 (1882) (tax on telegrams placed into interstate commerce an unconstitutional direct interference with interstate commerce).

The holding of *Utah Power & Light Co.* v. *Pfost*, 286 U.S. 165 (1932) does not compel a contrary result. First, as previously discussed, the tax here at issue is, an

actual operation and intended effect, a tax on the interstate transmission of electrical energy, quite unlike the tax in *Utah Power*.

Second, the nature of the electrical utility industry has changed dramatically since *Utah Power* was decided in 1932. What was once an industry characterized by small companies operating almost entirely within their service area, with only occasional, isolated interstate activity, has become a nation-wide energy system. Indeed, the creation of this national electrical energy system has been fostered and made possible by Congressional assistance. The clearest expression of the need for and desirability of a national electrical network is set forth in the Federal Power Act, 16 U.S.C. Section 824(a) (1935).

> For the purpose of assuring an abundant supply of electrical energy throughout the United States with the greatest possible economy and with regard to the proper utilization and conservation of natural resources, the [Federal Power] Commission is empowered and directed to divide the country into regional districts for the voluntary interconnection and coordination of facilities for the generation, transmission, and sale of electric energy, and it may at any time thereafter, upon its own motion or upon application, make such modifications thereof as in its judgment will promote the public interest.

Interstate coordination of energy transmission and sale is a relatively recent phenomenon that advances the Congressional objective of economical and reliable sale of electrical energy to consumers. To produce energy which is as economical as possible, the producers of electricity have taken advantage of "economies of scale" by building enormous generating facilities unheard of in 1932.[1] These modern facilities produce lower cost electricity than would otherwise be available by being built close to the source of fuel and water, by requiring fewer transmission and related facilities, etc. These savings are made possible by the fact that technological advances in the past 40 years now allow transmission of enormous quantities of electrical energy over long distances. However, to take advantage of economies of scale, plants of the requisite capacity must be jointly owned and interconnected with other generating facilities in order to meet the goal of reliability. The interconnecting system and joint-ownership of large facilities provides essential security against the risk of a utility being unable to supply its consumers with energy in the event of a single generating facility failure. It is in this context that the business of generating electricity has become totally interstate in nature and fact.

The New Mexico tax, if sustained, could seriously distort this essential pattern of interstate electrical energy development. The scientific and engineering realities of the electric industry, which were used as the basic test in *Connecticut Light & Power Co.* v. *Federal Power Commission*, 324 U.S. 515 (1945) should lead this Court to conclude that the New Mexico tax is a tax on interstate commerce rather than a tax on the "local" activity of generating electricity in New Mexico. *See Fisher's Blend Station Inc.*, v. *Tax Commission*, 297 U.S. 650 (1936).

The effect of this tax discrimination falls directly upon the citizens of Arizona who consume energy produced in and exported from New Mexico. Arizona utilities, with one minor exception, retail their electrical energy only to consumers in Arizona. For that reason, Arizona utilities incur no liability to New Mexico for its gross receipts tax which is incurred at the point of retail sale. The credit is unavailable to Arizona utilities; the generation tax therefore must be paid and added to the cost of doing business in Arizona.

The tax borne by the Arizona utilities is inevitably passed on to Arizona consumers. Unlike taxes imposed upon unregulated manufacturers and producers of goods and products, a tax imposed on a regulated entity has a predictable incident. Two of the Arizona entities subject to the electrical energy tax are investor-owned public service corporations subject to regulation by the Arizona Corporation Commission. As such, under the decisions of this Court, these entities must be permitted to charge rates reasonably calculated to permit them to recover operating expenses (including expenses in the nature of the electrical energy tax) and earn a fair rate of return on behalf of stockholders, a result mandating the eventual pass-through of the electrical generation tax to residents of Arizona. *See Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Bluefield Water Works & Improvement Co.* v. *Public Service Commission*, 262 U.S. 679 (1923). The third entry, Salt River Project, is both an integral part of a Federal reclamation project and a political subdivision of the State of Arizona; any costs incurred in producing electrical energy will reflect directly in charges to Arizona residents who use water and power from the project.

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[1]For example, the Four Corners Generating Plant located in New Mexico and owned by utilities located in Arizona, California, New Mexico and Texas, generated 11.777 billion kilowatt hours of energy in 1974; or nearly 12 percent of the 99.359 billion kilowatt hours of energy consumed in the United States in 1932.

The discriminatory nature of the tax violates the interstate Privileges and Immunities Clause of Article IV of the United States Constitution, which provides: "The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States." In *Austin* v. *New Hampshire*, 420 U.S. 656 (1975), a case richly suggestive of the situation here confronted, the State of New Hampshire had contrived a "commuter tax" which obstensibly applied both to out-of-State residents working in New Hampshire and New Hampshire residents working outside the State. However, by virtue of a series of exemptions and credits analogous to the tax credit for gross receipts taxes paid in connection with New Mexico retail sales in this case, the overall effect of the statute was a tax payable only by out-of-State residents. In striking down the tax, this Court concluded:

II. The Act Denies to Arizona Citizens the Privileges and Immunities Guaranteed by Article IV of the United States Constitution and Denies Equal Protection of the Laws in Violation of the Fourteenth Amendment to the United States Constitution.

Taxation schemes that impose special burdens on nonresidents come within an area of special concern to this Court. *Allied Stores, Inc.* v. *Bowers*, 358 U.S. 522, 532–33 (1959) (Separate opinion). Tax classifications by State Legislatures which turn upon residence are subject to "a standard of review substantially more rigorous than that applied to State tax discrimination among, say, forms of business organizations or different trades and professions." *Austin* v. *New Hampshire*, 420 U.S. 656 (1975). Furthermore, any presumption that exists in favor of the validity of State tax classifications disappears when the State Legislature enacting the statute in question has declared its discriminatory purpose, *Wheeling Steel Corp.* v. *Glander*, 337 U.S. 562 (1949).

As previously shown, the Act establishes a discriminatory classification by means of the credit provision which exempts from taxation all electricity consumed in New Mexico and taxes only electricity consumed outside New Mexico. Moreover, there is no question that the statute was intended to place the tax on nonresidents. (See the letter and attached computations submitted herewith as Appendix "B", from Commissioner of Revenue O'Cheskey to Senator Aubrey Dunn, dated March 10, 1975, advising the sponsor of the Act of precisely how the rate of tax provision and credit provision embodied in the Act should be structured to avoid imposition of any tax burden whatsoever on New Mexico residents.)

> The Privileges and Immunities Clause, by making noncitizenship or nonresidence an improper basis for locating a special burden, implicates not only the individual's right to nondiscriminatory treatment but also, perhaps more so, the structural balance essential to the concept of federalism. Since nonresidents are not represented in the taxing State's legislative halls, (citation omitted) judicial acquiescence in taxation schemes that burden them particularly would remit them to such redress as they could secure through their own State; but "to prevent (retaliation) was one of the chief ends sought to be accomplished by the adoption of the Constitution." 420 U.S. 662–63 (citing *Travis* v. *Yale & Towne Manufacturing Co.*, 252 U.S. 60,80 (1920).

In *Toomer* v. *Witsell*, 334 U.S. 385 (1948), the Court held invalid South Carolina statutes imposing disproportionate taxes on nonresident shrimp trawlers. The Court confronted a situation suggestive of the retaliatory war that will predictably occur if the electrical energy tariff is allowed to take root, stating:

> Restrictions on non-resident fishing in the marginal sea, and even prohibitions against it, have now invited retaliation to the point that the fishery is effectively partitioned at the state lines, bilateral bargaining on an official level has come to be the only method whereby any one of the States can obtain for its citizens the right to shrimp in waters adjacent to the other States. 344 U.S. at 388.

If, in the midst of a national energy crisis, the 50 states are given license to break up and dislocate a national system of electrical distribution through the use of export tariffs, the resulting disaster would dwarf the problems incurred by the shrimping industry prior to the *Toomer* decision.

By parity of reasoning, the New Mexico tax also violates the Equal Protection Clause of the Fourteenth Amendment. *Wheeling Steel Corp.* v. *Glander*, 337 U.S. 562 (1949) (Ohio tax statute discriminating against nonresident corporations held to violate Equal Protection Clause, the Court stating "the federal right of a nonresident 'is the right to equal treatment"). *Cf. Travellers Insurance Co.* v. *Connecticut*, 185 U.S. 364 (1902).

The class of Arizona residents designated by the New Mexico Legislature as the ultimate bearer of the New Mexico tax cannot be justified under even the most liberal deference to possible legislative motives or policies. The New Mexico tax, when viewed in light of the industry to which it relates and its statutory history, declares and effects its discrimination purpose as clearly as the statute struck down by this Court in *Wheeling Steel.*

CONCLUSION

For the foregoing reasons, leave should be granted to file the proposed complaint.

Respectfully submitted, Bruce E. Babbitt, 159 State Capitol, Phoenix, Arizona, Arizona Attorney General.

APPENDIX "A"

STATE OF NEW MEXICO, BUREAU OF REVENUE, SANTA FE, N. MEX.

MARCH 10, 1975

Memorandum

To: Hon. Aubrey Dunn,
New Mexico State Senator.

From: Fred L. O'Cheskey, commissioner, Bureau of Revenue.

Subject: S-258—Electrical Energy Tax Act.

This is in reply to your inquiry in which you requested sample calculations relative to effects of this tax on utilities in New Mexico and ultimately to the consumers.

For example, let's say a utility is generating 200 million net KWH in New Mexico in a given month. The generation tax would be $80,000. Historically, the breakdown of consumption in New Mexico is as follows:

	Percent
*Commercial and Industrial	66.0
*Residential	24.0
Sales—Other public authority	6.8
*Irrigation	1.5
Public street and highway lighting	1.0
Sales—Interior Department	0.5
Sales—Military	0.2
Total	100.0

Of this breakdown, the consumption items shown with an asterisk would be that portion subject to the gross receipts tax and totals 91.5 percent. Applying this to the 200 million KWH generated less average line loss of 2.5 percent yields 195 million net KWH for sale. If the utility has the States average taxable consumption of 91.5 percent subject to the gross receipts tax and the average price per KWH is 1.8 cents then the total gross receipts would be 178.4 million KWH times 1.8 cents equals $3.212 million with $128,466 [1] in gross receipts tax ordinarily due. The $80,000 in generation tax can be offset by the utility against the gross receipts tax ordinarily due of $128,466. The utilities customers' billing would remain the same, with the usual "passed on" gross receipts tax of 4 percent.

If the generating utility sells to other utilities in the state, the generation tax can be assigned along the route with the buyer reimbursing the utility generating the electricity for the generation tax. The ultimate retailer of the electricity can credit the generation tax against the gross receipts tax. Under the generation tax rate of ½ mill per/KWH, of all the utilities in New Mexico, it appeared that only Southwestern Public Service Company might have to pass some generation tax on to New Mexico consumers. It appears that the amendment to four tenths of a mill brings down the generation tax so that even in Southwestern's case the gross receipts tax more than offsets the generation tax.

FRED L. O'CHESKEY,
Commissioner of Revenue.

[Exhibit B was subsequently supplied by another witness and appears at p. 60 of this volume.]

[1] This amount of gross receipts tax is much larger in most cases since the tax also applies on the "fuel clause adjustment which varies from 10 percent to 50 percent of the basic cost of electricity.

EXHIBIT C

NEW MEXICO STATUTES

ANNOTATED

REPLACEMENT VOLUME 10, PART 2 1975 POCKET SUPPLEMENT. PUBLISHED UNDER THE SUPERVISION OF THE NEW MEXICO COMPILATION COMMISSION

Amendments to Acts and New Laws Enacted by the Legislature Since Publication of Replacement Volume 10, Part 2, and Annotations Supplementing the Replacement Volume, and The Standards of Title Examination of the State Bar of New Mexico.

72-33-11. Sale of property to pay tax.—A personal representative may sell so much of any property as is necessary to pay the taxes due under the Estate Tax Act [72-33-1 to 72-33-12]. A personal representative may sell so much of any property specifically bequeathed or devised as is necessary to pay the proportionate amount of the taxes due on the transfer of the property and the fees and expenses of the sale, unless the legatee or devisee pays the personal representative the proportionate amount of the taxes due.

History: Laws 1973, Ch. 345, Section 11.

72-33-12. Liability for failure to pay tax before distribution or delivery.—A. Any personal representative who distributes any property without first paying, securing another's payment of, or furnishing security for payment of the taxes due under the Estate Tax Act [72-33-1 to 72-33-12] is personally liable for the taxes due to the extent of the value of any property that may come or may have come into his possession. Security for payment of the taxes due under the Estate Tax Act shall be in an amount equal to or greater than the value of all property that is, or has come into the possession of such personal representative, as of the time such security is furnished.

B. Any person who has the control, custody or possession of any property and who delivers any of the property to the personal representative or legal representative of the decedent outside New Mexico without first paying, securing another's payment of, or furnishing security for payment of the taxes due under the Estate Tax Act is liable for the taxes due under the Estate Tax Act to the extent of the value of the property delivered. Security for payment of the taxes due under the Estate Tax Act shall be in an amount equal to or greater than the value of all property delivered to the personal representative or legal representative of the decedent outside New Mexico by such a person.

History: Laws 1973, ch. 345, Section 12.

Title of Act.—An act relating to taxation; providing for an estate tax with respect to decedents dying on or after July 1, 1973; enacting the Estate Tax Act; amending and repealing certain sections of the NMSA 1958.—Laws 1973, ch. 345.

Temporary Provision—Savings Clause.—Section 15 of ch. 345, Laws 1973 read: "The Estate Tax Act does not apply to transfers of the net estates of decedents who die prior to July 1, 1973. Any taxes, the liability for payment of which was incurred by reason of events occurring prior to the effective date of the provisions of the Estate Tax Act, shall be paid, collected and enforced as provided by statutes in force at the time the events occurred."

ARTICLE 34—ELECTRICAL ENERGY TAX ACT

Section 72-34-1.—Short title.
Section 72-34-2.—Definitions.
Section 72-34-3.—Imposition of tax—Rate—Denomination as electrical energy tax.
Section 72-34-4.—Measurement and recording of kilowatt hours of electricity.
Section 72-34-5—Reports—Remittances.
Section 72-34-6—Relief from other taxes.

72-34-1. Short title.—Sections 1 through 6 of this act [72-34-1 to 72-34-6] may be cited as the "Electrical Energy Tax Act."

History: Laws 1975, ch. 263, Section 1.

Compiler's Notes.—This act became effective July 1, 1975.

Title of Act.—An act relating to taxation; imposing a tax on the generation of electricity; amending sections 45-4-28 and 72-13-24 NMSA 1953 (being Laws 1939, chapter 47, section 28 and Laws 1965, chapter 248, section 12, as amended); enacting a new section 72-16A-16.1 NMSA 1953.—Laws 1975, ch. 263.

Cross-References—Tax Administration Act applicable, 72-13-14.

Utility Supplement Act payments withheld pending challenge to Electrical Energy Tax Act, 13-20-9.

72-34-2. Definitions.—As used in the Electrical Energy Tax Act [72-34-1 to 72-34-6]:

A. "bureau" means the New Mexico bureau of revenue; B. "generation" includes manufacture and production; C. "electricity" includes electrical energy and electrical power; D. "person" means any individual, estate, trust, receiver, co-operative association, electric co-operative, club, corporation, company, firm, partnership, joint venture, syndicate, association, irrigation district, electrical irrigation district and any utility owned or operated by a county or municipality, and also means to the extent permitted by law, any federal, state or other governmental unit of subdivision or an agency, department or instrumentality; and E. "sale" means selling or transferring to any person for consumption, use or resale and includes barter and exchange.

History: Laws 1975, ch. 263, Section 2.

72-34-3. Imposition of tax—Rate—Denomination as electrical energy tax—A. For the privilege of generating electricity in this State for the purpose of sale, whether the sale takes place in this State or outside this state, there is imposed on any person generating electricity a temporary tax, applicable until July 1, 1984, of four-tenths of one mill ($.0004) on each net kilowatt hour of electricity generated in New Mexico.

B. The tax imposed by this section shall be referred to as the "electrical energy tax."

History: Laws 1975, ch. 263, Section 3.

72-34-4. Measurement and recording of kilowatt hours of electricity.—Persons subject to the imposition of the electrical energy tax shall maintain accurate measuring devices and records to measure and record the daily and cumulative monthly and yearly totals of kilowatt hours of electricity generated or distributed in this state.

History: Laws 1975, ch. 263, Section 4.

72-34-5. Reports—Remittances.—Every person subject to the imposition of the electrical energy tax shall file a return on forms provided by and with the information required by the bureau and shall pay the tax due on or before the twenty-fifth day of the second month following the month in which the taxable event occurs.

History: Laws 1975, ch. 263, Section 5.

72-34-6. Relief from other taxes.—Unless otherwise specified by statute the imposition of the electrical energy tax shall not act to relieve any person or activity from any other tax levied by the state of New Mexico or its political subdivisions.

History: Laws 1975, ch. 263, Section 6.

Nonseverability Clause.—Section 10 of ch. 263, Laws 1975 provided: "LEGISLATIVE INTENT.—It is the intent of the legislature that this entire 1975 act be considered not severable, and should any part hereof be declared unconstitutional, the entire act should be declared void."

EXHIBIT D

New Mexico Statutes

ANNOTATED

Replacement Volume 10, Part 2

1975 Pocket Supplement, published under the supervision of the New Mexico Compilation Commission.

Amendments to Acts and New Laws Enacted by the Legislature Since Publication of Replacement Volume 10, Part 2, and, Annotations Supplementing the Replacement Volume and, The Standards of Title Examination of the State Bar of New Mexico.

The fact, that there are only four block manufacturers who are customers of corporation leasing machinery does not make the transaction "occasional" or "isolated" under subsection G of 72-16-2 (since repealed), and a conclusion that the corporation was not "engaging" in business did not follow. Besser Co. v. Bureau of Revenue, 74 N.M. 377, 394 P.2d 141, 146.

Legislative Intent

The legislature in enacting the Emergency School Tax Act intended to tax the privilege of conducting businesses by miners, manufacturers, public utilities, contractors, operators of amusement, enterprises, operators of business services, factors, brokers and agents and to exempt sales to United States, state agencies, societies, hospitals and fraternal and religious organizations not for profit. Dikewood Corp. v. Bureau of Revenue, 74 N.M. 75, 390 P. 2d 661, 664.

Although the legislature changed "full sale price" to "Full sale contract amount" in subsection F, it did not intend to tax that which was not received or never would be received as evidenced by the fact that the phrase "cash discount allowed and taken" is excluded from the definition of "gross receipts." Davis v. Commissioner of Revenue, 83 N.M. (App.) 152, 489 P. 2d 660.

Nature of Tax.

While the Emergency School Tax Act may be called a "sales tax," the legislature and the Supreme Court have properly called it a "privilege tax." Dikewood Corp. v. Bureau of Revenue, 74 N.M. 75, 390 P. 2d 661, 664.

Sales at Retail.

The receipts of a corporation, which leased machinery to four New Mexico users, were taxable as sales at retail within the meaning of subsection H of 72-16-2 (since repealed). Besser Co. v. Bureau of Revenue, 74 N.M. 377, 394 P. 2d 141, 145.

Sales for Consumption.

The definition of "consumption" contained in subsection I of 72-16-2 (since repealed) had no application where tax was imposed upon gross receipts from leasing of machinery. Besser Co. v. Bureau of Revenue, 74 N.M. 377, 394 P. 2d 141, 145.

Time Price Differential.

Where taxpayer made credit installment sales on contract, receiving a down payment and selling the contract to a finance company which furnished the contract form and approved the credit of the purchasers before the contracts were executed and paid the taxpayer the total cash sales price minus the amount he received as a down payment, and the taxpayer did not receive and never would receive any time-price differential, such amount was not "gross receipts" to him. Davis v. Commissioner of Revenue, 83 N.M. (App.) 152, 489 P. 2d 660.

72-16A-4. Imposition and rate of tax—Denomination as "gross receipts tax."—A. For the privilege of engaging in business, an excise tax equal to four percent [4 percent] of gross receipts is imposed on any person engaging in business in New Mexico.

B. The tax imposed by this section shall be referred to as the "gross receipts tax."

History: Laws 1966, ch. 47, Section 4; 1969, ch. 144, Section 2.

Amendments.

The 1969 amendment increased the tax imposed by subsection A from three per cent to four per cent of gross receipts.

Opinions of Attorney General.

1967-68, Nos. 67-97, 67-135, 68-36.

Application.

Where services performed for other banks' accounts were not reasonably necessary or incidental to functions or business of national banking association, state was not precluded from levying gross receipts tax on association's receipts collected for such services by federal law since association could pass tax on to banks for which it performed such services and therefore association was not real taxpayer. First Nat. Bank of Sante Fe v. Commissioner of Revenue, 80 N.M. (App.) 699, 460 P. 2d 64, cert. den. 80 N.M. 707, 460 P. 2d 72, appeal dismissed 397 U. S. 661, 25 L. Ed. 2d 643, 90 S. Ct. 1407.

Engaging in Business.

Nonprofit corporate taxpayer which engaged in business for the benefit of members, but not for the benefit of corporation itself, was not engaging in business within the meaning of this statute. American Automobile Assn., Inc. v. Bureau of Revenue, 87 N. M. 330, 533 P. 2d 103, reversing 86 N.M. (Appl.) 569, 525 P. 2d 929.

EXHIBIT E

NEW MEXICO STATUTES

ANNOTATED

Replacement volume 10, Part 2.

1975 Pocket Supplement, published under the supervision of the New Mexico Compilation Commission.

into contract on April 7 was entitled to benefit of temporary provision, its rights not being waived by failure to attempt registration under the invalid regulation. R. H. Fulton, Inc. v. New Mexico Bureau of Revenue, 85 N. M. (App.) 583, . . . P. 2d 1079.

DECISIONS UNDER FORMER LAW

Constitutionality. Subsection D of 72-16-5 (since repealed), which prior to 1963 amendment, exempted gross receipts from any lump-sum or unit price contract for a particular project entered into prior to March 31, 1961, if the contract would not by its terms allow the contractor to increase his price to cover any additional privilege tax which was to be levied against him, did not offend Const., art. II, . . . and art. VII, Section 1 requiring equal protection and uniformity of taxation Gruschus v. Bureau of Revenue, . . . M. 775, 399 P. 2d 105, 108.

72-16A-16. Credit—Compensating tax.—A. If on property bought outside this state, a gross receipts, sales, compensating or similar tax has been levied by another state or political subdivision thereof on the transaction by which the person using the property in New Mexico acquired the property and such tax has been paid, the amount of such tax paid may be credited against any compensating tax due this state on the same property.

B. When the receipts from the sale of real property constructed by a person in the ordinary course of his construction business are subject to the gross receipts tax, the amount of compensating tax previously paid by the person on materials which became an ingredient or component part of the construction project and on construction services performed upon the construction project, may be credited against the gross receipts tax due on the sale.

History: Laws 1966, ch. 47, Section 16; 1973, ch. 342, Section 1.

Title of Act.

An act relating to taxation; amending section 72-16A-16 NMSA 1953 (being Laws 1966, chapter 47, section 16) to provide a credit against gross receipts taxes on receipts from the sale of certain real property for compensating taxes paid on certain construction materials and services furnished in connection with a construction projectl—Laws 1973, ch. 342.

Amendments.

The 1973 amendment designated the former section as subsection A and added subsection B.

Effective Date.

Section 2 of ch. 342, Laws 1973 read: "The effective date of the provisions of this act is July 1, 1973."

Saving Clause.

Section 18 of ch. 47, Laws 1966 read: "The Gross Receipts and Compensating Tax Act does not apply to any taxable event that occurred prior to its effective date. The payment, collection or enforcement of taxes, the liability for payment of which was incurred by reason of events occurring prior to the effective date of the Gross Receipts and Compensating Tax Act, is to be accomplished according to the provisions of the applicable statutes previously in force in every manner as though the Gross Receipts and Compensating Tax Act had not been enacted." Section 17 of ch. 47, Laws 1966 [72-16A-17] was repealed by Laws 1975, ch. 116, Section 6.

72-16A-16.1. Credit—Gross receipts tax.—A. If on electricity generated outside this state and consumed in this state, an electrical energy tax or similar tax on such generation has been levied by another state or political subdivisions thereof, the amount of such tax paid may be credited against the gross receipts tax due this state.

B. On electricity generated inside this state and consumed in this state which was subject to the electrical energy tax, the amount of such tax paid may be credited against the gross receipts tax due this state.

C. The credit under subsections A or B of this section shall be assigned to the person selling the electricity for consumption in New Mexico on which New Mexico gross receipts tax is due, and the assignee shall reimburse the assignor for the credit.

History: C. 1953, Section 72-16A-16.1 enacted by Laws 1975, ch. 263, Section 9.

Nonservability Clause.

Section 10 of ch. 263, Laws 1975 provided: "LEGISLATIVE INTENT.—It is the intent of the legislature that this entire 1975 act [72-34-1 to 72-34-6] be considered not severable, and should any part hereof be declared unconstitutional, the entire act should be declared void."

72-16A-17. Repealed.

Repeal.

Section 72-16A-17 (Laws 1966, ch. 47, . . . 17), making it unlawful to advertise that tax was not a part of price of property or service sold, was repealed by Laws 1975, ch. 116, Section 6.

Effective Date.

Section 11 of ch. 263, Laws 1975 read: "The effective date of the provisions of this act is July 1, 1975."

72-16A-18. Cross references.—Any section of the New Mexico Statutes Annotated, 1953 Compilation, that refers to the emergency school tax, the Emergency School Tax Act, the compensating tax or the Compensating Tax Act of 1939 shall be construed to refer to the Gross Receipts and Compensating Tax Act [72-16A-1 to 72-16A-19], the Resources Excise Tax Act [72-16A-20 to 72-16A-29] or the Liquor Excise Tax Act [46-7-15 to 46-7-22], whichever is appropriate.

History: Laws 1966, ch. 47, Section 19.

72-16A-19. Compiling instructions.—The Gross Receipts and Compensating Tax Act [72-16A-1 to 72-16A-19] shall be compiled as Article 16(A) of Chapter 72 of the New Mexico Statutes Annotated. The Resources Excise Tax Act [72-16A-20 to 72-16A-29] shall be compiled in Article 16(A) of Chapter 72 of the New Mexico Statutes Annotated following the Gross Receipts and Compensating Tax Act.

History: Laws 1966, ch. 47, Section 20.

Separability Clause.

Section 21 of ch. 47, Laws 1966 read: "To insure orderly and efficient collection of the public revenue, if any part of application of the Gross Receipts and Compensating Tax Act is held invalid, the remainder of the Gross Receipts and Compensating Tax Act or its application to other situations or persons shall not be affected."

Repealing Clause.

Section 22 of ch. 47, Laws 1966 repealed 72-16-2 through 72-16-19 and 72-17-1 through 72-17-7.1.

Effective Date.

Section 23 of ch. 47, Laws 1966 read: "The effective date of the Gross Receipts and Compensating Tax Act shall be July 1, 1967."

Senator GRAVEL. Our next witness is Mr. B. D. Johnson, executive manager, Accounting and Control, Virginia Electric and Power Co., Richmond, Va.

STATEMENT OF BILL D. JOHNSON, EXECUTIVE MANAGER, ACCOUNTING AND CONTROL, VIRGINIA ELECTRIC AND POWER CO.

Senator GRAVEL. Mr. Johnson, please proceed as is comfortable for you.

Mr. JOHNSON. Thank you, Mr. Chairman.

Mr. Chairman and members of the committee, my name is Bill D. Johnson, and I am executive manager, Accounting and Control, for Virginia Electric and Power Co., VEPCO.

I am appearing here today to endorse what Senate Bill 1957 seeks to accomplish.

VEPCO has been faced with the problem enumerated in Senate bill 1957 for several years now because of the Company's operation of a generating plant in West Virginia.

VEPCO operates a coal-fired electric generating plant at Mt. Storm in Grant County, W. Va. This station supplies power to consumers in three States: Virginia, West Virginia, and North Carolina.

Approximately 3 percent of the electricity generated at this plant is sold in West Virginia with the remaining 97 percent carried over high voltage transmission lines to serve VEPCO's customers in Virginia and North Carolina.

Presently, VEPCO pays to the State of West Virginia a business and occupation tax imposed upon electric utilities measured by the sales and demand charges as to electric power sold in West Virginia.

As to all other electricity generated at Mount Storm, and transmitted outside the State of West Virginia, VEPCO pays a manufacturer's tax of 88 cents per $100 of valuation.

In 1975, the tax paid to West Virginia upon the manufacture of electricity in excess of sales in West Virginia amounted to $955,000. The magnitude of the tax for a given year depends to some degree upon the generation for that year.

In 1976, we estimate that this tax will approximate $1.5 million based on the current rate of 88 cents per $100 of valuation.

When this tax was first imposed by the State of West Virginia upon VEPCO, we sought relief in the Supreme Court of Appeals of West Virginia on the basis, among other things, that the levy of such a tax was a burden upon interstate commerce forbidden by the Constitution of the United States.

After failing to get relief in that court, we sought relief in the U.S. Supreme Court but that Court declined to hear the case.

Two weeks ago, a bill was introduced in the West Virginia Legislature to change the current tax rate of 88 cents per $100 of valuation on electricity generated in West Virginia and transmitted outside the State to $5.72 per $100 of valuation, an increase of 550 percent in the tax rate.

Following the appearance of VEPCO and other utilities operating in West Virginia, in opposition to this bill, Senate bill 572, it was amended to place the tax rate at $3 per $100 of valuation, still an increase of 241 percent in the tax rate.

Therefore, under the current proposal, VEPCO's tax on electric power generated in West Virginia and exported out of the State would increase from approximately $1.5 million estimated for 1976 to approximately $5.1 million, based upon current generation levels.

The present tax rate on electricity sold to retail customers within West Virginia is $5.72 per $100 of gross receipts. Another feature of this bill would also reduce the tax rate to $3 per $100 of gross receipts on sales within West Virginia. I am informed subsequent to this testimony being prepared that this bill was passed on Saturday night by a vote of 33 to one in the West Virginia Senate and the rate was revised to take the tax off residential consumers entirely.

Therefore, the result of the West Virginia proposed legislation as we understand it is to reduce the cost of electricity to West Virginia residential consumers by reducing the West Virginia tax burden which is borne by West Virginia customers at the expense of consumers in the neighboring states.

If such a tax method is permitted to continue, there is no limit as to what level the tax could be imposed on electricity users outside of the State at the will of the West Virginia Legislature.

Accordingly, it is clear that the West Virginia business and occupation tax on electric power generated in the State discriminates against

VEPCO's customers in Virginia and North Carolina in favor of all electric customers in West Virginia, the majority of whom we do not serve.

It places an undue burden on our Virginia and North Carolina customers since this generation, when sold, is taxed again at 3½ percent of gross receipts when sold in Virginia and at a 6 percent tax rate on gross receipts when sold in North Carolina.

Senate Bill 572 now before the West Virginia Legislature would serve to increase this burden upon interstate commerce.

To subject the generation of electricity exported to a manufacturing tax rate of $3 per $100 of valuation while the rate applied to all other manufacturing in the State of West Virginia is 88 cents per $100 of valuation is discriminatory and, in my judgment, a clear burden upon interstate commerce.

Indeed, the proposal would appear to violate several provisions of the Federal Constitution as was pointed out by our Counsel in his appearance before the West Virginia Legislature in opposition to this proposal. Our counsel pointed out that:

1. It would seem to violate clause 3, section 8, article 1, which reserves to the Congress, alone, the power "to regulate commerce with Foreign Nations, and among the several States."

2. It would seem to violate section 10 of article 1, which provides that "no State shall, without the consent of Congress, lay any imposts or duties on imports or exports."

3. It would seem to violate the provisions of article IV, section 2, which provides that "the citizens of each State shall be entitled to all privileges and immunities of citizens in the several States," and, finally.

4. It would seem to violate the 14th Amendment to the U.S. Constitution which provides that no State shall deprive any person of life, liberty or property without due process of law; nor deny any person, within its jurisdiction, the equal protection of the law.

Many cases could be cited that discriminatory taxes or retraints upon commerce, whatever their form, violate the purpose and the intent of the Federal Constitution.

The West Virginia proposal, in the guise of a tax, is nothing more than electric utility rate regulation by the West Virginia Legislature which would serve to reduce intrastate rates financed by an increase in the utility rates charged to citizens of a neighboring state.

As we all know, the New Mexico Legislature, in July 1975, attempted to tax the generation of electricity exported which caused the State of Arizona to bring action in the U.S. Supreme Court.

Unless action is taken to prevent States from engaging in such activities, as here described, it is not difficult to look into the future and see the possible consequences that will result.

1. Utilities will seek increased rates to reflect increased costs of services to their customers because of the tax structure of neighboring States.

2. States may well follow the lead of Arizona and institute legal proceedings in the U.S. Supreme Court to enjoin collection of this discriminatory tax or seek refund thereof.

3. Regulatory commissions may defer action on rate relief sought by utilities until the matter is settled by the U.S. Supreme Court.

4. Citizens and legislators of one state may well become bitter and explore ways in which they can retaliate against their neighboring States either by government or private action and, finally,

Throughout all this period of time the legal disputes are being resolved, electric utilities and their customers will be caught in the middle of this dispute which will injure the utilities' financial position and may well jeopardize their ability to render reliable service.

Accordingly, Mr. Chairman, we ask that this committee recommend to the Congress that Senate bill 1957 be enacted into law.

Thank you.

Senator FANNIN [presiding]. Thank you, Mr. Johnson.

Certainly, in your last reference, reference five, page five, you bring out there the great need for action to be taken one way or the other, so that all parties involved will know just exactly where they stand.

I commend you for bringing that out so forcefully to the committee.

Do we understand correctly that in addition to the West Virginia tax the electricity generated at Mount Storm also is taxed by the State where it is consumed; that is, Virginia or North Carolina?

Now, I think you made some statements there about the changes in the legislation that is involved in the West Virginia Legislature, but could you answer the question for me?

Mr. JOHNSON. Yes.

When the power coming from our generating plant in West Virginia, after having been taxed by West Virginia, is sold in Virginia, it is again taxed at 3½ percent of the proceeds therefrom.

In North Carolina, when it is sold, it is taxed again at the rate of 6 percent of gross receipts.

So, it does, in effect, result in double taxation of that same power.

Senator FANNIN. Mr. Johnson, why does a utility such as VEPCO build a generating plant in a State that imposes a tax on generation such as the West Virginia tax?

Mr. JOHNSON. When we built Mount Storm in West Virginia, it was then for the purpose of locating the plant near the coal supply, even though it required high voltage transmission lines to get that power to our load centers. The economies were still present at that time.

Subsequent thereto, this battle began in the State of West Virginia as to the taxation of this power. To be sure, Senator, the tax burden on that power has now reduced those economies or made them non-existent.

Senator FANNIN. Thank you very much, Mr. Johnson. We very much appreciate your testimony.

Mr. JOHNSON. Thank you, sir.

Senator FANNIN. The next witness is Mr. Fred O'Cheskey, commissioner of revenue for New Mexico, accompanied by Mr. Jan Unna, assistant attorney general of New Mexico from Santa Fe.

Welcome, gentlemen, to the hearings. I understand you do not have a statement to present to the committee; that is, a written statement?

STATEMENT OF FRED L. O'CHESKEY, COMMISSIONER OF REVENUE, STATE OF NEW MEXICO, ACCOMPANIED BY JAN UNNA, ASSISTANT ATTORNEY GENERAL, STATE OF NEW MEXICO

Mr. O'CHESKEY. That is correct. I do have a statement and I will provide a written statement shortly to the committee.

Senator FANNIN. All right. The committee will appreciate that if you will do that, you may proceed as you think best.

Mr. O'CHESKEY. I am Fred O'Cheskey, Commissioner of Revenue of New Mexico and also the Secretary of Taxation and Revenue for the State.

I am here in opposition essentially to Senate bill 1957. The New Mexico Electrical Energy Tax Act imposes a tax on the privilege of generating electricity in New Mexico for the purpose of sale at the rate of four-tenths of a mill per kilowatt-hour generated.

Under this act it makes no difference whether the person generating is a New Mexico corporation or a corporation organized under another state's statutes. The tax is the same; it is imposed on that utility generating in the State of New Mexico.

This is not a unqiue tax, as you heard. West Virginia, the States of Washington, Idaho and South Carolina, to name a few, have imposed similar taxes on electricity or the manufacture of same.

Senator FANNIN. You say to name a few. You certainly have a list of all of them. I am sure you came prepared to give them if there are more than just the ones you have stated. I would like to know them.

Mr. O'CHESKEY. I believe there are eight. I have not completed my research. There are some differences in the tax but I named four of the States that I am aware of.

Senator FANNIN. Thank you, sir.

Mr. O'CHESKEY. In order to understand this tax, I think it is helpful to understand State taxing system in New Mexico.

New Mexico imposes a very broadly based sales tax or gross receipts tax on all goods and services for final consumpticn within the State, including medical services, drugs, legal services, contract services, and all types of tangibles including food.

So, I think from that brief list you can see that we have a very broadly based tax and this came about primarily because New Mexico is a sparsely populated State and really must have a broadly based tax in order to provide the governmental services.

New Mexico makes maximum use of all taxes and all taxing methods, including income tax, property tax, and all of your traditional consumptive taxes such as the tax on gasoline, severance taxes on major minerals, et cetera.

The New Mexico taxing system provides for a credit against our tax on similar imposition by another State or its political subdivisions on the same transaction.

This is generally true in terms of a tax on a commodity taxed in one other State; it can be credited against our gross receipts or sales tax, so that double taxation essentially is relieved.

This law is generally designed to maximize the tax and yet eliminate duplications.

In designing the electrical energy tax, the legislature, in its wisdom, decided to prevent duplication by allowing a credit against the State gross receipts or sales tax for the amount of electrical energy tax it imposed by New Mexico or another state if that other State imposes a similar tax.

Senator FANNIN. May I ask a question at this time?

Mr. O'CHESKEY. Surely.

Senator FANNIN. Is it not correct that the practical effect of the New Mexico electrical energy tax is to shift the incidence of tax to the interstate transmitting outside New Mexico?

Mr. O'CHESKEY. The tax is imposed on all generation and it is credited so that the New Mexico citizens are not paying a higher rate than they were previously.

Persently, they are paying 4 percent on the gross receipts as compared to four-tenths of a mill on the generation tax.

So, they are paying a much higher tax at 4 percent to 4½ percent.

Senator FANNIN. How would a resident of Arizona get a refund on that tax under the present law?

How could he get the refund on that tax?

Mr. O'CHESKEY. The resident of Arizona essentially has this tax passed on to him, the generation tax.

I believe that the Corporation Commission in Arizona is allowing the pass-through but the amount is——

Senator FANNIN. But the thing about it is that in New Mexico you get the tax refund, You can apply it against your gross receipts tax.

Mr. O'CHESKEY. In New Mexico that tax is at 4 percent or 4½ percent already, and the State did not want to impose additional taxes on its citizens.

Senator FANNIN. You are evading the question. You are treating the people of New Mexico differently than you are treating the people of the States in which the product is exported.

Mr. O'CHESKEY. Well, Mr. Chairman, I did want to make it clear that New Mexico citizens are paying a substantial tax presently.

Senator FANNIN. Well, they are not getting a refund on it. They are not getting a refund on their tax; is that what you are saying?

Mr. O'CHESKEY. The utility is allowed to credit the generation tax either passed on to them by a person generating in New Mexico or if Arizona had a generating tax——

Senator FANNIN. We are talking about practical operations existing today.

The people in Arizona cannot get a refund of the tax under present law; the people of New Mexico can get a refund.

Mr. O'CHESKEY. No, the people——

Senator FANNIN. The consumers of the product in New Mexico could get a refund; the consumers of the product in Arizona cannot get a refund.

Mr. O'CHESKEY. The consumers in New Mexico do not get a refund, Mr. Chairman.

Senator FANNIN. They can apply it to the tax that they owe, however.

Mr. O'CHESKEY. The taxpayer; the utility is allowed to credit generation tax against gross receipts tax——

Senator FANNIN. So, they are getting a credit for it.

Mr. O'CHESKEY. That is correct, a credit.

Senator FANNIN. Is there any comparable tax of which you are aware sanctioned by the courts or the Congress which permits any state to export the incidents of its tax?

Mr. O'CHESKEY. Yes, Mr. Chairman. I am aware of a number of states that—in my record, in my presentation, if I could go forward, I will point out a number of other States that impose similar manufacturing taxes. I have a list of those.

Senator FANNIN. My question was: Sanctioned by the courts or the Congress.

Mr. O'CHESKEY. Sanctioned by the courts, Mr. Chairman.

Senator FANNIN. Not the Congress?

Mr. O'CHESKEY. Congress has allowed States to impose taxes on local incidents. For example, in Alaska, they are able to—they have a cannery tax, which is essentially manufacturing or canning salmon.

Many States——

Senator FANNIN. This is interstate commerce, which is certainly control of interstate commerce.

Mr. O'CHESKEY. I believe your question went to the fact that do other states have other kinds of taxes which essentially the——

Senator FANNIN. Would compare with what we are discussing here today?

Mr. O'CHESKEY. Yes, there is.

For example, Wyoming has a tax on cement which they manufacture in their State; they have a manufacturing tax which, essentially, is passed on in the price to other States which——

Senator FANNIN. They don't tax their own people?

Mr. O'CHESKEY. They tax their own people.

Senator FANNIN. And their own people—well, is there any refund or anything involved as far as people of Wyoming?

Mr. O'CHESKEY. I am not aware of the particular tax.

Senator FANNIN. No.

Mr. O'CHESKEY. There are a host of taxes where the impact is essentially exported.

Senator FANNIN. On March 10, I understand, of last year, you wrote to State Senator Aubrey Dunn of New Mexico that by reducing the generation tax rate to four-tenths of a mill the entire burden of this tax would be more than offset by a credit against New Mexico's gross receipts tax for New Mexico utilities.

Isn't this a rather clear indication of where New Mexico's legislature wanted the incidents of this tax to fall?

Mr. O'CHESKEY. The New Mexico Legislature, in my view, and I would say that this tax was a legislative initiative program; this tax was essentially—the credit was allowed and that letter or memo you were referring to was provided as a tax reduction or essentially a rate reduction during the legislative session from five-tenths of a mill to four-tenths of a mill.

That was essentially to prevent duplication or essentially to allow this credit to work in New Mexico so that additional taxes would not have to be passed on other than the present four percent gross receipts tax to customers. That is a true statement.

Senator FANNIN. Well, you may proceed with your statement.

Mr. O'CHESKEY. In designing the electrical energy tax, the legislature decided to prevent duplication by allowing a credit against the sales tax for that amount of electrical energy tax imposed by New Mexico or if a similar tax is imposed by another State, allow a credit against that tax.

I would like to point out, as I did earlier, that this was a legislative initiative item and not a taxation initiated item, if you will.

The need for the funds generated by the electrical energy tax, I think, is very important to consider. New Mexico rated last year 48th lowest State in per capita income nationally.

We can hardly get much lower. With 1.1 million population of New Mexico, we are having the same kind of problems other states are having in financing roads, and financing energy-related construction.

The chairman is very familiar with the Four Corners area of New Mexico. There are very few railroads, if any; no long-distance communications to speak of; very poor roads; in fact, one of the sites for the coal gasification development is on Indian land and presently there is a four-wheel drive road to that particular site.

The funds from the electrical energy tax are to be used essentially to provide energy-related roads in the Four Corners area.

The electrical energy tax would generate $4 million a year to improve or develop roads and it has an automatic repealer of 1984 when enough money would be provided through the tax in order to finance approximately $25 million of expenditures in road construction.

This tax underscores the problems energy States are having generally in financing much needed facilities and services related to energy development.

I think it points up the extreme problem of financing energy boom-town situations and the associated problems for States.

We in New Mexico are generally attempting to deal with the problems and, of course, are having our difficulties. As this committee is fully aware, there is a great need to finance public improvements demanded by increasing energy development and poorer States like New Mexico are attempting to do so by essentially taxing the companies that are, if you will, extracting the energy production.

The burdens on energy production states of the pollution problems, reclamation of lands, consumption of water, consumption of fuel resources generally is tremendous.

The options available in financing needs are minimal other than the ones I have stated. If State and local governments go through the bonding route with long-term bonds financed with severed materials such as coal, oftentimes the projection of the reserves is shorter than the projection in paying off the bonds.

So, there are problems in going other routes.

Another use of this electrical energy tax, $1.3 million annually, is to assist recipients of Federal supplemental security income benefits and recipients of the aid to families with dependent children in meeting increased costs for gas and electrical utility bills.

So, really, the use of the money is twofold: highway construction and to supplement the funds available to the aged, blind, and disabled on their increased utility rates which they are, of course, having to pay.

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I would like to reemphasize that the 4 percent statewide gross receipts tax applies to electrical energy sold at retail. We also have approximately 32 municipalities that impose a one-fourth of 1 percent gross receipts tax and we have three counties that impose a one-fourth of 1 percent gross receipts tax.

These are imposed on utilities, on the electrical energy and gas the same as any other commodity. So, in effect, you have consumers in New Mexico paying 4½ percent in many areas on the utility bills presently.

An energy tax is critical, as we have discussed, but I would like to point out that the sales tax is much higher than the energy tax.

The credit provision was placed on the same bill as the section imposing the tax to make it a very straightforward method of attacking the problem.

The intention of the New Mexico Legislature was—with respect to electrical energy generated and sold by utilities in New Mexico—that the transactions be taxed only once.

This is why the provision exists, the credit provision, to allow the electrical energy tax to be credited against gross receipts tax so we essentially tax the energy only once.

In New Mexico we have in effect imposed a manufacturers' tax very similar to the type of tax other States have imposed on manufactured goods.

For example, in Hawaii, the State imposes a number of manufacturer-type taxes on many types of products, a very broadly based tax, and they, of course, tax it under their sales tax.

West Virginia—we have already discussed that.

The State of Washington; North Dakota has a tax on coal conversion plants, which is essentially a manufacturers' type tax like ours.

Vermont, Alaska—we talked about a tax on canneries, which is essentially a manufacturers' tax.

You find your whisky States tax their commodity, whisky, that they produce, and the impact gets exported to other States.

Montana, and a host of States, have similar manufacturers' taxes.

The very existence of a tax on commodities does not really mean that they are all undue burdens on interstate commerce.

New Mexico's tax structures, with respect to the electrical energy tax, is not distinguishable constitutionally from the electrical energy tax cases, Public Utility District Two, *Washington*-case, South Carolina Power Co., and I won't read all these cases, but there are a number of cases which we have argued——

Senator FANNIN. Do any pertain to electrical power?

Mr. O'CHESKEY. Two of the cases do. Other cases, such as liquor cases——

Senator FANNIN. I know——

Mr. O'CHESKEY. Apply to credit provisions similar to what New Mexico has in which they credit against an ultimate sales tax.

Senator FANNIN. There is a lot of kick in the liquor business and that doesn't apply like the power and sales tax.

Mr. O'CHESKEY. There is the *Old-Time Distiller's* case, but there were a number of credit cases which do support New Mexico's credit and have gone to the U.S. Supreme Court previously.

Senator FANNIN. I do not have any knowledge of anything that is comparable to the energy tax that has gone to the Supreme Court.

If you have something specific on that, I would like it for the record.

Mr. O'CHESKEY. South Carolina Power, Public Utility District No. 2.

Senator FANNIN. Can you give me the exact case?

Mr. O'CHESKEY. This is a Washington case. You don't——

Senator FANNIN. You don't have the exact case?

Mr. O'CHESKEY. I will furnish in my statement the exact citation.

[The case referred to follows:]

Public Utility District No. 2 of Grant County v. *State of Washington*, 82 Wh.2d 232, 510 P.2d 206 (1973), app. dism'd for want of a substantial Federal question, 414 U.S. 1106 (1973).

Senator FANNIN. Thank you.

Mr. O'CHESKEY. These cases establish the tax burden imposed on different incidents of taxation and must be considered together in resolving the discrimination issue.

The electricity-oriented cases, which I spoke of previously, held that there is no discrimination against interstate commerce if the commodity of commerce—here electrical energy—is subject to equivalent taxation by the State whether or not the ultimate use and consumption is within or without the state.

It is our view that the Electrical Energy Tax Act does not burden interstate commerce. The generation of electricity is a local activity which New Mexico may tax.

There is also a *Utah Power and Light* versus *Pfost* case. The U.S. Supreme Court held that in this case the tax did not, as to electricity, transmit it outside the taxing state, being Idaho, imposing an unconstitutional burden on interstate commerce.

Senator FANNIN. I think you have quoted some cases—that was back in 1934. I think you are having a difficult time coming up with something comparable to what we are talking about, but go ahead.

Mr. O'CHESKEY. In conclusion, we would hope that Congress would not take drastic action to preclude States from taxing one form of manufacturing.

In a time of massive financial problems for States such action would only aggravate greater problems. I would hope the action taken would not be a single shot, such as the electrical energy tax, but possibly look at the broad spectrum of manufacturing taxes.

I appreciate very much, Mr. Chairman, the time you have allotted today and thank you for allowing the time for this presentation.

Senator FANNIN. Thank you.

May I ask this question: Is the State of New Mexico having any concern for the effect that this tax will have on the possible retaliatory action which other States in the Southwest might take?

Mr. O'CHESKEY. The credit provision provides, as I indicated, if another State has a similar tax, for example—I know that Arizona is looking at nuclear power and I dare say that in 30 or 40 years when our coal runs out we will be possibly using nuclear power from Arizona.

If Arizona had such a tax, it would be credited against our gross receipts tax.

Senator FANNIN. I would just say from the standpoint of what is being considered, I don't think that Arizona will have the tax, but that is something that neither one of us know what will take place, but the effect such a tax could have on the further development of multi-State generating facilities is another consideration.

What is the opinion on that?

Mr. O'CHESKEY. Well, I, of course, don't really have an opinion on the generation question. As I say, this was a legislative initiated tax and I don't know all of the considerations that went into the matter.

I can appreciate the problem of large-scale generation, having worked for a utility in my previous experience, that it is an important factor.

Senator FANNIN. Some of your people have referred to this as a temporary tax. Do you refer to it as a temporary tax?

Mr. O'CHESKEY. Yes, I do. Within the provisions of the act it calls for a repealer in 1984.

Senator FANNIN. Do you think that it will be repealed in 1984?

Mr. O'CHESKEY. Yes. The consideration was in passing the bill that it would generate approximately $25 million, which hopefully could be matched with Federal funds to essentially build roads on the reservation lands.

Senator FANNIN. Well, you talk about the need for funds.

We will get to the roads in a moment.

The need for funds will be over in 1984; is that your testimony?

Mr. O'CHESKEY. What the legislation calls for.

Senator FANNIN. Do you believe that?

Mr. O'CHESKEY. I believe that. I can't speak for our legislature.

Senator FANNIN. I know but why would you say that when you poor-mouth New Mexico to the extent where that, you know, you feel sorry for them and you want to see what you can do.

I was Governor of Arizona and I had competition with New Mexico and very, very tough competition for industry and New Mexico dragged down—that was the Chamber of—or Industrial Welcoming Board—they talked about New Mexico being one of the richest States in the United States from the standpoint of natural resources

How can you account for that?

Mr. O'CHESKEY. Well, it is rich from the standpoint of natural resources——

Senator FANNIN. Oil producing. Where do you——

Mr. O'CHESKEY. It does not result in increased per capita income, I am sorry to say.

Senator FANNIN. You have the opportunity for that, but you are going to make other States develop your own resources.

Where do you stand on that as far as oil production is concerned?

Is New Mexico fourth or fifth?

Mr. O'CHESKEY. I believe New Mexico is seventh and our production is declining every year. The only thing that saved our revenues were the price increases, but production, as such, both in oil and gas industries, is essentially a falling pattern.

Senator FANNIN. Of course, I have had testimony from New Mexico that if they could just get gas deregulated, we could get a great deal more gas from New Mexico.

You mean that is a false statement?

Mr. O'CHESKEY. No, that would occur if you had more exploration. The price does affect the amount of exploration.

Senator FANNIN. The gas is there?

Mr. O'CHESKEY. The gas is there but it is probably not being produced because of the low price.

Senator FANNIN. That is my point. But deregulation I was told would bring on increased production and we would be able to get gas for Arizona; we don't have any.

Mr. O'CHESKEY. I am sure it would probably help. Price increases would have the effect of increasing exploration.

Senator FANNIN. Are you aware that the Four Corners Commission has provided considerable funds for roads on the reservations?

Mr. O'CHESKEY. I am not aware of that. Do you recall the amount?

Senator FANNIN. You are aware that considerable money has been provided for roads on the reservations by the Four Corners Commission?

Mr. O'CHESKEY. How much as been provided?

Senator FANNIN. I am asking if you are aware of the funds being provided for the reservation's roads.

Mr. O'CHESKEY. I am not aware of the magnitude we are talking about here, which is——

Senator FANNIN. Of course, I don't know the magnitude you are talking about here because New Mexico does not have the obligation to provide the roads on reservation.

Mr. O'CHESKEY. We feel we do have an obligation. Many of these roads are both on and off the reservation.

Senator FANNIN. Now you are talking about something else. New Mexico does not have the obligation to provide roads on the reservations.

If it is interstate highway or something of that nature then, of course, that's a Federal program with the State maintaining the roads, but that is one matter.

If you talk about new roads, that is another matter.

Mr. O'CHESKEY. We are attempting to work with tribal leaders on a generalized road system for the area. Of course, it doesn't really help in that isolated area, the chairman is fully aware, to have roads just on the reservation because they need to get to the population centers.

Senator FANNIN. Of course, as I am sure you know, you probably travelled around the reservations and certainly it has been my privilege to travel on the reservations, both in New Mexico and Arizona, and I am very familiar with the needs of the Navajos expecially, because they have the largest reservation involved.

So, I feel that the main thoroughfares are—it is just to tie up the roads that are involved and the roads that are leading out to some of the natural resources that you are talking about.

Of course, on the reservations I don't think the revenue from that source is of great benefit to the State of New Mexico but it certainly is of great benefit to the Indian people.

Mr. O'CHESKEY. Mr. Chairman, you have been over those roads. There is a concern by tribal leaders that many of the Indian-related deaths are because of the poor road conditions. There are quite a few dips and they are quite narrow and there have been a large

number of deaths on these particular roads, so that the concern is not just whether the road exists but also the safety factors.

They are quite poor, I think.

Senator FANNIN. Don't you consider that the Federal Government has that obligation rather than the State of New Mexico?

Mr. O'CHESKEY. We are attempting to use this money to match——

Senator FANNIN. The money coming from this source?

Mr. O'CHESKEY. We are attempting to use the electrical energy tax dollars to match Federal funds when they become available——

Senator FANNIN. For your road programs?

Mr. O'CHESKEY. For the road programs.

Senator FANNIN. Not necessarily on the Indian reservations?

Mr. O'CHESKEY. Both on and off. I understand there are funds that might be available to provide matching funds for just Indian land-related roads.

Senator FANNIN. Well, if you could furnish the committee with information in that regard, I would appreciate it, although I don't think that that is necessary from the standpoint of need when you talk about the need for funds. [The information referred to above may be found in Mr. O'Cheskey's prepared statement, marked as exhibit C.]

Senator FANNIN. I think we are getting beyond the equities involved when we are talking about the rich use necessary of electrical energy taxes.

I just feel that you are mixing apples with oranges when you are talking about that.

I do appreciate your testimony.

I don't agree with your arguments, but I hope you will furnish the information to verify some of the statements you have made in regard to these suits and rulings from the Supreme Court or any other courts that would be of benefit to the members of the committee.

We certainly want to be fair. At the same time, I think we are opening up a problem that could be very widespread and have serious consequences. Like you said, the State of Arizona could start this same type of program, but it is no more right for the State of Arizona to do it than it is for the State of New Mexico.

So, I would discourage the State of Arizona from doing it.

Mr. O'CHESKEY. I appreciate your courtesy, Mr. Chairman.

Thank you.

Senator FANNIN. Fine, thank you. We appreciate your coming to testify.

[The prepared statement of Mr. O'Cheskey follows. Oral testimony continues on p. 66]

STATEMENT BY FRED L. O'CHESKEY, COMMISSIONER OF REVENUE, STATE OF NEW MEXICO

Mr. Chairman and members of the committee; My name is Fred L. O'Cheskey. I am Commissioner of Revenue and Secretary of Revenue and Taxation for the State of New Mexico.

NEW MEXICO'S ELECTRICAL ENERGY TAX ACT

The New Mexico Electrical Energy Tax[1] imposes a tax on the privilege of generating electricity in New Mexico for the purpose of sale at the rate of 4/10 of one mill per kilowatt hour generated. The tax applies equally to all persons generating electricity.

[1]Chapter 263, Laws 1975 (see Exhibit A attached).

This generation tax is not unique to New Mexico. The states of Alabama, Idaho, Louisiana, South Carolina, Washington and West Virginia have had such a tax on their books for quite a few years.

The state of New Mexico has a very broadly based gross receipts tax which taxes all goods and services sold within the state. For example, New Mexico taxes medical services, drugs, food, legal services and construction services to name a few. New Mexico also makes use of other forms of taxes including income, property, gasoline and severance taxes on natural resources such as oil and gas.

The generation tax must be read together with the gross receipts tax. Receipts from the sale of electricity at retail in New Mexico are taxed at the minimum rate of 4 percent. In most populous areas the rate of the tax is 4½ percent. For example in Santa Fe, the seller is taxed at 4 percent as a state gross receipts tax, one-fourth of 1 percent as municipal gross receipts tax and one-fourth of 1 percent as a county gross receipts tax.

The Electrical Energy Tax Act was designed to avoid pyramiding of taxation of electricity sold in New Mexico. The legislature provided that the electrical energy tax may be credited against the gross receipts tax. Indeed it provided that any generation tax, whether levied by New Mexico or a sister state, could be credited against the gross receipts tax. In this manner New Mexicans would not be forced to pay more than a 4½ percent tax on the electricity they consume.

NEED FOR THE GENERATION TAX

New Mexico was 48th in per capita income in 1975. The coal deposits used to generate electricity are located in the Four Corners Area. Utilities have found it profitable to locate massive generating plants there. They also use vast amounts of New Mexico's most precious commodity, water. They benefit from lower transportation costs and the absence of population centers which would necessitate more costly pollution control devices. The area is quite isolated and undeveloped. No railroad serves it; distances between commercial centers are quite great and the roads are few and in relatively poor shape. Many are suited only for four wheel drive vehicles. The prospect of it becoming an "energy boom" area looms in the future because of the extensive low-sulfur coal deposits present in the area.

Needless to say, the demand for state services everywhere is great, but it is even greater for the Four Corners area. Much needed improvements in the area's basic infrastructure are necessary. State services for this area need to be expanded. To finance this increase, the New Mexico legislature enacted the generation tax. It rests on the principle that those who benefit from the natural resources removed from the state should in return pay a share of the cost of state supported services.

USE OF THE ELECTRICITY ENERGY TAX

The Electrical Energy Tax Act provides that one-half the monies derived from the electrical energy tax be set aside in an electrical energy tax fund. At the same time the generation tax was enacted, the New Mexico Legislature also appropriated $32 million from this fund to the State Highway Commission for the construction and improvement of highways and roads in the Four Corners Area.[2] It was hoped that this state revenue could be matched with Federal funds for the improvement of State Road 44, State Road 371, and U.S. 666. These badly needed improvements have the support of the Navajo Nation.[3]

In addition, under the N.M. Utility Supplement Act, the electrical energy tax is to be used to make direct payments of approximately $1.3 million annually to certain aged, blind and disabled residents to cover the rising cost of their utility bills.[4]

THE CONSTITUTIONALITY OF THE ELECTRICAL ENERGY TAX ACT

New Mexico's Electrical Energy Tax Act is the subject of two constitutional attacks. The first proceeding is an original action filed by Arizona in the U.S. Supreme Court to have the Act declared unconstitutional under the Commerce, Privileges and Immunities and Equal Protection Clauses of the U.S. Constitution.[5] The Second is a suit by Arizona, California and Texas utilities generating electricity in New Mexico but selling it outside the state.[6] They claim that the tax is violative of the U.S. and

[2]Chapter 145, Laws 1975 (see Exhibit B).

[3]See Exhibit C.

[4]Chapter 300, Laws 1975 (see Exhibit D).

[5]*Arizona* v. *New Mexico*, No. 70 Orig., U.S. Sup. Ct. (see Exhibit E for New Mexico's brief filed in this case).

[6]*Arizona Public Service Co., et al.* v. *Fred L. O'Cheskey, et al.*, No. 50245, District Court for Santa Fe County, New Mexico.

N.M. Constitutions. Both of these proceedings are pending, but neither court has issued any rulings yet.

The utilities and the State of Arizona claim that the Act discriminates against them because the tax may be credited against gross receipts tax. New Mexico contends that its tax statutes with respect to electrical energy do not discriminate unconstitutionally against anyone.

We believe that the judicial proceedings begun by Arizona and its utilities should be allowed to run their course. Only after they have been concluded will the Act's constitutional status under existing law be clarified. It is possible that the tax may be struck down, in which case there would be no need for S.B. 1957.

CONCLUSION

It has been settled for over four decades that the generation of electricity is a local event which the states are free to tax.[7] S.B. 1957 would single out electricity among all forms of energy and make its production part of interstate commerce, thus removing it from the states' tax base. Oil production, gas production and mining are other local energy producing activities that have long been taxed by the states. An Arizona consumer buying fuel oil to heat his house may indirectly pay a Texas, Oklahoma, or Alaska tax on severing oil. An Arizona consumer may indirectly pay a Wyoming or Montana severance tax on the coal he uses to heat a boiler. Yet S.B. 1957 does not single out any one of these state's taxes and declare it unconstitutional. Why the discriminatory treatment of electricity? Alaska taxes fish frozen and shipped to the Arizona consumer.[8] New Mexico's tax on generation is merely the tax on the manufacture of electricity, which is a local incident.

S.B. 1957 would remove all electrical energy production from the states' tax reach. New Mexico, like West Virginia and other states, has power companies which do nothing in New Mexico but generate electricity. They exploit New Mexico's natural resources and benefit from many other services and privileges afforded by New Mexico. S.B. 1957 would allow them to enjoy this status without paying the state in return. Such a drastic consequence is unwarranted. That is why we oppose S.B. 1957.

THE LEGISLATURE OF THE STATE OF NEW MEXICO, 32D LEGISLATURE, 1ST SESSION, LAWS 1975

CHAPTER 263

AN ACT RELATING TO TAXATION; IMPOSING A TAX ON THE GENERATION OF ELECTRICITY; AMENDING SECTIONS 45-4-28 AND 72-13-24 NMSA 1953 (BEING LAWS 1939, CHAPTER 47, SECTION 28 AND LAWS 1965, CHAPTER 248, SECTION 12, AS AMENDED); ENACTING A NEW SECTION 72-16A-16.1 NMSA 1953.

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

Section 1. SHORT TITLE.—Sections 1 through 6 of this act may be cited as the "Electrical Energy Tax Act".

Section 2. DEFINITIONS.—As used in the Electrical Energy Tax Act:

A. "bureau" means the New Mexico bureau of revenue;

B. "generation" includes manufacture and production;

C. "electricity" includes electrical energy and electrical power;

D. "person" means any individual, estate, trust, receiver, cooperative association, electric cooperative, club, corporation, company, firm, partnership, joint venture, syndicate, association, irrigation district, electrical irrigation district and any utility owned or operated by a county or municipality, and also means to the extent permitted by law, any Federal, state or other governmental unit or subdivision or an agency, department or instrumentality; and

E. "sale" means selling or transferring to any person for consumption, use or resale and includes barter and exchange.

Section 3. IMPOSITION OF TAX—RATE—DENOMINATION AS ELECTRICAL ENERGY TAX.—

A. For the privilege of generating electricity in this state for the purpose of sale, whether the sale takes place in this state or outside this state, there is imposed on any person generating electricity a temporary tax, applicable until July 1, 1984, of four-tenths of one mill ($.0004) on eah net kilowatt hour of electricity generated in New Mexico.

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[7] *Utah Power & Light Co.* v. *Pfost*, 286 U.S. 165 (1932).

[8] *Alaska* v. *Arctic Maid*, 366 U.S. 199 (1961).

B. The tax imposed by this section shall be referred to as the "electrical energy tax".

Section 4. MEASUREMENT AND RECORDING OF KILOWATT HOURS OF ELECTRICITY.—Persons subject to the imposition of the electrical energy tax shall maintain accurate measuring devices and records to measure and record the daily and cumulative monthly and yearly totals of kilowatt hours of electricity generated or distributed in this state.

Section 5. REPORTS—REMITTANCES.—Every person subject to the imposition of the electrical energy tax shall file a return on forms provided by and with the information required by the bureau and shall pay the tax due on or before the twenty-fifth day of the second month following the month in which the taxable event occurs.

Section 6. RELIEF FROM OTHER TAXES.—Unless otherwise specified by statute the imposition of the electrical energy tax shall not act to relieve any person or activity from any other tax levied by the state of New Mexico or its political subdivisions.

Section 7. Section 45-4-28 NMSA 1953 (being Laws 1939, Chapter 47, Section 26, as amended) is amended to read:

"45-4-28. TAXATION.—Cooperative and foreign corporations, transacting business in this state pursuant to the provisions of Sections 45-4-1 through 45-4-32 NMSA 1953 shall pay annually, on or before July 1, to the state corporation commission, a tax of ten dollars ($10.00) for each one hundred persons or fraction thereof to whom electricity is supplied within this state which tax shall be in lieu of all other taxes except those provided in the Gross Receipts and Compensating Tax Act, and the Electrical Energy Tax Act; provided, however, that in the event a contract has been entered into by a rural electric cooperative and a power consumer prior to February 1, 1961, and such contract does not contain an escalator clause providing for an increase for added tax liability on the cooperative, then the sale to such power consumer shall be exempt until the expiration, extension or renewal of the contract."

Section 8. Section 72-12-24 NMSA 1953 (being Laws 1965, Chapter 248, Section 12, as amended) is amended to read:

"72-13-24. RECEIPTS—DISBURSEMENTS—DISTRIBUTION.—

A. All money received by the bureau shall be deposited with the state treasurer before the close of the next succeeding business day after receipt of the money.

B. Money received or disbursed by the bureau shall be accounted for by the commissioner as required by law or regulation of the director of the department of finance and administration.

C. Disbursements for tax credits, refunds and the payment of interest shall be made by the department of finance and administration upon request and certification of their appropriateness by the commissioner or his delegate. The state treasurer shall create a suspense fund for the purpose of making the disbursements authorized by the Tax Administration Act. All revenues collected pursuant to the provisions of Sections 72-15-1 through 72-15-37 NMSA 1953, the Income Tax Act, the Withholding Tax Act, the Gross Receipts and Compensating Tax Act, the Resources Excise Tax Act, the Liquor Excise Tax Act and the Electrical Energy Tax Act shall be credited to this suspense fund and are appropriated for the purpose of making disbursements for tax credits, refunds and the payment of interest.

D. On the last day of each month, any money remaining in the suspense fund after the necessary disbursements have been made shall be identified by tax source and transferred from the suspense fund, one-half of the receipts attributable to the electrical energy tax shall be transferred to the 'electrical energy fund', hereby created, and the remainder to the state general fund, except that before the remaining money is transferred to the general fund, and amount equal to one percent of the taxable gross receipts reported for the month of deposit:

(1) for each municipality shall be distributed to each municipality; and

(2) by taxpayers who have business locations on an Indian reservation of pueblo grant in an area which is contiguous to a municipality and in which the municipality performs services pursuant to a contract between the municipality and the Indian tribe or Indian pueblo shall be distributed to the municipality if:

(a) the contract describes the area in which the municipality is required to perform services and requires the municipality to perform services that are substantially the same as the services the municipality performs for itself; and

(b) the governing body of the municipality has submitted a copy of the contract to the commissioner of revenue.

E. Disbursements to cover expenditures of the bureau shall be made only upon approval of the commissioner or his delegate.

F. Miscellaneous receipts from charges made by the bureau to defray expenses pursuant to the provisions of Sections 72-13-23 and 72-13-39 NMSA 1953 and similar charges are appropriated to the bureau for its use."

Section 9. A new Section 72-16A-16.1 NMSA 1953 is enacted to read: "72-16A-16.1.

CREDIT—GROSS RECEIPTS TAX.—

A. If on electricity generated outside this state and consumed in this state, an electrical energy tax or similar tax on such generation has been levied by another state or political subdivisions thereof, the amount of such tax paid may be credited against the gross receipts tax due this state.

B. On electricity generated inside this state and consumed in this state which was subject to the electrical genergy tax, the amount of such tax paid may be credited against the gross receipts tax due this state.

C. The credit under Subsections A or B of this section shall be assigned to the person selling the electricity for consumption in New Mexico on which New Mexico gross receipts tax is due, and the assignee shall reimburse the assignor for the credit."

Section 10. LEGISLATIVE INTENT.—It is the intent of the legislature that this entire 1975 act be considered not severable, and should any part hereof be declared unconstitutional, the entire act should be declared void.

Section 11. EFFECTIVE DATE.—The effective date of the provisions of this act is July 1, 1975.

CHAPTER 145

AN ACT MAKING AN APPROPRIATION FOR THE CONSTRUCTION OR IMPROVEMENT OF CERTAIN HIGHWAYS IN THE NORTHWESTERN SECTION OF THE STATE.

Be it enacted by the Legislature of the State of New Mexico:

Section 1. ELECTRICAL ENERGY FUND APPROPRIATION—ALLOCATION—LIMITATION.—

A. receipts attributable to the electrical energy tax transferred to the electrical energy fund in an aggregate amount not to exceed thirty-two million dollars ($32,000,000) are appropriated to the state highway commission for the construction or improvement of New Mexico roads 44 and 371, United States highway 666 and roads designated N-36 and RD-3005 within the state of New Mexico.

B. Upon the certification of need by the state highway commission, the department of finance and administration may allocate to the state highway commission money appropriated in Subsection A of this section to the extent of the balance in the fund, the aggregate amount of all allocations not to exceed thirty-two million dollars ($32,000,000).

C. Allocation of this appropriation shall be conditioned upon the certification by the state highway commission that agreements have been entered into between the state highway commission and the United States government, the governing authority of Indian tribes who have jurisdiction over the lands on which the roads are located, or private enterprises having an interest in the construction or improvement of the roads, or any combination of the three, providing for cooperation and matching funds in the financing of construction of or improvements to the roads. The state's share of the cost of construction and improvement projects to which appropriations are made in this act shall not exceed the following percentages:

(1) New Mexico road 44, fifty percent;

(2) New Mexico road 371, fifty percent;

(3) United States highway 666, fifty percent; and

(4) N-36 and RD-3005, thirty-three and one-third percent each.

THE NAVAJO NATION,
WINDOW ROCK, ARIZONA,
June 18, 1975.

MR. JULIAN GARCIA,
Chairman, New Mexico State Highway Commission,
Santa Fe, N. Mex.

DEAR MR. GARCIA: On June 16, 1975, I met with members of the Four Corners Transportation Committee to discuss priorities on road improvements and construction in northwestern New Mexico, mainly state roads 371, 44 and U.S. 666. The needs for major road improvements are substantial, for example, the Navajo Agricultural Products Industries will be in operation by 1976. This development alone will require additional road systems to accommodate agricultural activities and associated activities. Also within a couple of years the proposed coal gasification plants will very likely be under construction and the ultimate operation of these gasifiers within three years

after. In order to accommodate the traffic and as a measure of public safety, road improvements in this major development area must be accelerated to synchronize with the needs of proposed industrial activities.

As you know the State of New Mexico authorized $27,000,000 to fund the subject three major road improvements and construction, and the Federal Government also passed legislation authorizing $25,000,000 to match the state's $27,000,000. I would like to inform you that the Navajo Tribe and the Four Corners Transportation Committee are in full agreement on how the $52,000,000 will be proportioned among the three highways, state 44, 371 and U.S. 666. It was agreed that 50% of the state and federal special funding would be allocated to highway 371; 35% to state highway 44 and the remaining 15% to U.S. 666.

I firmly believe it is to the mutual interest and benefit to the Navajo Tribe, county and state to unite their efforts in causing the Office of Management and Budget to immediately release $10,000,000 of the $25,000,000 (authorized special funding) as an amendment to the fiscal year 1976 federal budget. The communities of northwestern New Mexico, both Navajos and non-Indians, solicit your support to have these roads constructed and improved as soon as possible.

Sincerely yours,

WILSON C. SKEET,
Vice Chairman,
Navajo Tribal Council.

ARTICLE 20—UTILITY SUPPLEMENT ACT

13-20-1. Short title.—This act [13-20-1 to 13-20-9] may be cited as the "Utility Supplement Act."

History: Laws 1975, ch. 300, § 1, eff. July 1, 1975.

13-20-2. Legislative intent.—It is the intent of the legislature that the utility Supplement Act [13-20-1 to 13-20-9] be used to assist recipients of federal supplemental security income benefits and recipients of aid to families with dependent children in meeting increased costs for gas and electrical utilities to the maximum extent possible. The appropriation made in the Utility Supplement Act shall be used to generate those federal funds which may be available.

History: Laws 1975, ch. 300, § 2, eff. July 1, 1975.

13-20-3 Administration of Utility Supplement Act.—The health and social services department is hereby authorized to determine eligibility, to compute grants, make payments as provided in the Utility Supplement Act [13-20-1 to 13-20-9] and otherwise administer that act.

History: Laws 1975, ch. 300, § 3, eff. July 1, 1975.

13-20-4 Persons eligible for utility assistance.—A. A utility supplement, pursuant to the Utility Supplement Act [13-20-1 to 13-20-9] shall be provided to or on behalf of:

(1) those individuals who are identified to the health and social services department by the bureau of supplemental security income as recipients of supplemental security income under Title XVI of the Social Security Act, and who are not living in nursing homes or intermediate care facilities; and

(2) those individuals who are identified by the health and social services department as recipients of aid to families with dependent children, under section 13-17-9 NMSA 1953, unless the individual are living in circumstances which which do not require them to pay, either directly or indirectly, utility costs.

B. No more than one utility supplement per household may be paid under the Utility Supplement Act; Provided, however, supplemental security income recipients and recipients of aid to families with dependent children living in boarding home facilities shall be paid on an individual basis.

History: Laws 1975, ch. 300, § 4, eff. July 1, 1975.

13-20-5. Time of payments.—A. The initial payment under the Utility Supplement Act [13-20-1 to 13-20-9] shall be made by the health and social services department between December 1, 1975 and December 15, 1975 to those eligible under the Utility Supplement Act as of December 1, 1975. The initial payment shall be the equivalent of six (6) months of benefits under the Utility Supplement Act. In no case shall the initial payment be greater than fifty-nine dollars ($59.00).

B. Beginning with the month of January, 1976, and monthly thereafter, payments shall be made to those eligible for benefits under the Utility Supplement Act.

History: Laws 1975, ch. 300, § 5, eff. July 1, 1975.

13-20-6. Amount of payment.—The amount of the utility supplement payment shall be calculated by the health and social services department so that the entire amount of state and federal funds avialable to it under the Utility Supplement Act [13-20-1 to 13-20-9] shall be expended.

History: Laws 1975, ch. 300, § 6, eff. July 1, 1975.

13-20-7. Adjustments to meet rate increases.—A. The health and social services department shall annually review the rate schedules of gas and electric companies in this state provided by the public service commission and, if necessary, shall recommend to the legislature adjustments in the amount of state utility supplements to reflect any increases or decreases in gas or electricity rates, or both.

B. The department shall conduct its first rate review during the month of December, 1975, and during the same month annually thereafter.

History: Laws 1975, ch. 300, § 7, eff. July 1, 1975.

13-20-8. Termination of state supplemental program.—The right to benefits under the Utility Supplement Act [13-20-1 to 13-20-9] shall terminate when any similar federal program becomes effective and the state participates in that program or the program shall terminate in 1984, whichever occurs first.

History: Laws 1975, ch. 300, § 8, eff. July 1, 1975.

13-20-9. No payment during injunction.—If the state should be sued by a party seeking to prohibit the collection of the tax provided for in the Electrical Energy Tax Act 72-34-1 to 72-34-6, no payments shall be made under the Utility Supplement Act 13-20-1 to 13-20-9 during the pendency of the suit and no payments shall be made if the Electrical Energy Tax Act is ultimately held invalid in any suit.

History: Laws 1975, ch. 300, § 10, eff. July 1, 1975.

No. 70 Original.

In the Supreme Court of the United States, October Term, 1975.

Arizona, Plaintiff, v. *New Mexico*, Defendant.

On Motion for Leave to File Original Action.

Brief in Opposition.

Toney Anaya, *Attorney General of New Mexico.*

Of counsel: Jan Unna, *Special Assistant Attorney General*, Daniel Friedman, *Special Assistant Attorney General*, Bureau of Revenue, P. O. Box 630, Santa Fe, New Mexico 87503.

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No. 70 Original.
Arizona, Plaintiff, v. *New Mexico*, Defendant.
On motion for leave to file original action.

BRIEF IN OPPOSITION

COUNTER-STATEMENT OF QUESTIONS PRESENTED

I. Should this Court exercise its original jurisdiction over a challenge by one state to tax the laws of another state if one of the plaintiff state's own political subdivisions and all other utilities of the plaintiff state upon which the legal incidence of the tax falls are already engaged in state legal proceedings against the tax will will dispose of all constitutional issues, and if neither the plaintiff state or its citizens will suffer any actual damage during the pendency of this state litigation?

II. Does the original jurisdiction of the Supreme Court extend to a challenge by a state to the tax laws of another state on the grounds that those laws infringe upon the federal constitutional rights of individual citizens and of electrical utilities doing business in the plaintiff state?

III. Does New Mexico's tax structure as to electrical energy violate the "equivalent taxation" rule reaffirmed by this Court in *Public Utility District No. 2 of Grant County* v. *State of Washington*, 82 Wn.2d 232, 510 P.2d 206 (1973), app. dism'd for want of a substantial federal question, 414 U.S. 1106 (1974)?

COUNTER-STATEMENT OF THE CASE

This action raises the question of the validity of one aspect of New Mexico's tax structure with respect to electrical energy.

Receipts from the sale of electricity are taxed under New Mexico's Gross Receipts and Compensating Tax Act, 72-16A-3, N.M.S.A. 1953 (1973 Supp.). The rate of the tax is 4 percent.

The New Mexico Electrical Energy Tax Act, Chapter 263, Laws 1975 (a copy of Chapter 263 is attached to Plaintiff's Complaint at p.8) imposes a tax on the privilege of generating electricity in New Mexico for the purpose of sale at the rate of four-tenths of 1 mill per kilowatt hour generated. The tax is nondiscriminatory on its face; it taxes all generation regardless of what is done with the electricity after generation.

The statutory provision which is the sole basis for plaintiff's theory of unconstitutional discrimination is contained in Sec. 72-16A-16.1(B) of the New Mexico Gross Receipts and Compensating Tax Act (Sec. 9B of Chapter 263, Laws 1975):

> "On electricity generated inside this state and consumed in this state which was subject to the electrical energy tax, the amount of such tax paid may be credited against the gross receipts tax due this state."

To illustrate the operation of this provision, assume, as is actually the case, Public Service Company of New Mexico (as well as numerous other utilities in New Mexico) generates and sells power at retail in New Mexico. It may credit the amount of the electrical energy tax it must pay to New Mexico against the *greater amount* of its New Mexico gross receipts tax liability. However, neither Arizona Public Service Co., nor Tucson Gas & Electric Co., nor Salt River Project, a political subdivision of Arizona (all Arizona utilities upon which the legal incidence of the generation tax falls, as it does upon New Mexico utilities generating electricity in New Mexico) will be able to take such a credit because their sales of power are outside the state. They have no New Mexico gross receipts tax liability against which to credit electrical energy tax. Thus, the practical effect of New Mexico's statutory scheme of taxation is to impose a tax no greater than 4 percent on the generation, production or distribution of electricity within New Mexico.

It is significant, as will be discussed in the argument following, that all three Arizona utilities have filed a declaratory judgment action in a New Mexico court claiming that the electrical energy tax is unconstitutional. Thus, all the issues Arizona wishes to raise in this forum will eventually come to this Court via appeal of the state proceedings.

ARGUMENT

I. Even Assuming That New Mexico's Tax Structure With Respect To Electrical Energy Is Arguably Unconstitutional, Which It Is Not, Arizona's Motion Should Be Denied Under Established Precedents Of This Court.

Arizona seeks to bring before this Court two causes of action against New Mexico. The first is proprietary in nature. It is based on two grounds: (1) Arizona is itself a consumer of electricity and will, it says, sustain an increased economic burden because New Mexico's electrical energy tax will be passed on to it* (Complaint,

*If it is passed on in the future, it will not be because New Mexico's generation tax requires it. The legal incidence of the tax is upon the generator; only the economic burden would then be on purchasers of electricity such as Arizona. See *First Agricultural Bank* v. *State Tax Commission*, 392 U.S. 339 (1967), *Gurley* v. *Rhoden*,—U.S.—, 95 S.Ct. 1605, 44 L.Ed.2d 110 (1975). Arizona's status in this respect, then, is no different from all consumers of goods or services who have at best a remote interest in the litigating of the validity of the tax.

first cause of action, VII and VIII). (2) Arizona's political subdivision, Salt River Project, generates electricity in New Mexico (Complaint, first cause of action, VI) and is subject to the generation tax.

Its second cause of action is as *parens patriae* for its citizens, to protect their alleged rights to be free of discrimination against interstate commerce and invidious classification.

In submitting that this Court should deny Arizona'a motion, we begin with the proposition that the Court will exercise its original jurisdiction only where it is clearly shown that resort to this extraordinary form of action is required. In its recent decision in *Illinois* v. *City of Milwaukee*, 406 U.S. 91, 93-94 (1972), the Court noted that:

> "It has long been this Court's philosophy that 'our original jurisdiction should be invoked sparingly.' . . . We construe 28 USC Sec. 1251(a)(1), as we do Art III, Sec. 2 cl 2, to honor our original jurisdiction but to make it obligatory-only in appropriate cases. And the question of what is appropriate concerns, of course, the seriousness and dignity of the claim; yet beyond that it necessarily involves the availability of another forum where there is jurisdiction over the named parties, where the issues tendered may be litigated, and where appropriate relief may be had. We incline to a sparing use of our original jurisdiction so that our increasing duties with the appellate docket will not suffer."

See also *Washington* v. *General Motors Corp.*, 406 U.S. 109 (1972).

The Court also has recently reaffirmed its view that disputes over the states' imposition of taxes ordinarily should not be entertained in an original action. In *Ohio* v. *Wyandotte Chemicals Corp.*, 401 U.S 493, 497 (1971), Justice Harland, speaking for the Court, said:

> "As our social system has grown more complex, the States have increasingly become enmeshed in a multitude of disputes with persons living outside their borders. *Consider, for example, the frequency with which States and nonresidents clash over the application of state laws concerning taxes*, motor vehicles, decedents' estates, business torts, government contracts, and so forth. *It would, indeed, be anomalous were this Court to be held out as a potential principal forum for settling such controversies.*" [Emphasis added.]

A. There Is Now Pending An Action In A New Mexico Court Brought By Arizona's Political Subdivision, Salt River Project, Arizona Public Service Co., And Tucson Gas & Electric Co. Which Will Effectively Dispose Of All Constitutional Claims Arizona Is Attempting To Bring Before This Court.

It is significant that Arizona asks for no monetary damages in its prayer for relief, only that the generation tax be declared unconstitutional. This is so because Arizona has not sustained any damages. The only way there could be any damage to Arizona itself or to its citizens is if the three Arizona utilities generating electricity in New Mexico are held liable for the tax. Then, says plaintiff, they will be allowed by plaintiff's own Corporation Commission (see A.R.S. Sec. 40-361 *et seq.*) to pass on the tax to consumers.

Although the first returns of electrical energy tax were due September 15, 1975, (Secs. 5, 11, Chapter 263, Laws 1975 [Complaint Exhibit "A"]), the three Arizona utilities chose not to pay the tax but to file a declaratory judgment action in the District Court for Santa Fe County, New Mexico, Case No. 50245. The Complaint alleges all the constitutional infirmities raised by Arizona in this action, and more.* Thus, the very same issues which Arizona asks this Court to review are being heard by a New Mexico court of general jurisdiction in the ordinary course of its business. If on appeal the New Mexico Supreme Court should hold the tax unconstitutional, Arizona will have been vindicated, and neither it nor its citizens will have been harmed because no Arizona utility will have paid New Mexico any tax during the pendency of the litigation. If the New Mexico Supreme Court holds the tax constitutional, the issues will come to this Court by way of direct appeal under 28 U.S.C. Sec. 1257 (2). If this Court upholds the tax, Arizona can, of course, have no cause of action against a constitutional tax. The action begun in the Santa Fe County District Court will ultimately dispose of all the contentions Arizona wishes this Court to hear now, and Arizona is participating in that action through its political subdivision, Salt River Project. There is, thus, no sound reason for this Court to hear Arizona's complaint, and this is especially true in view of the long-standing congressional and judicial policy

*A copy of the Complaint is printed in Appendix A attached hereto. A copy of New Mexico's motion to dismiss the Complaint is printed in Appendix B. This motion tests the constitutional merits of the Complaint. It also asks that the Court dismiss for lack of subject matter jurisdiction, which is merely a contention that the *forum* for litigating plaintiff's constitutional arguments should change to administrative proceedings under Sec. 72-13-38, N.M.S.A. 1953 (1973 Supp.) because the plaintiff's are not claiming a refund.

not to intervene in state tax matters. 28 U.S.C. Sec. 1341; *Great Lakes Dredge & Dock Co.* v. *Huffman*, 319 U.S. 293 (1943); *Toomer* v. *Whitsell*, 334 U.S. 385 (1948); *Matthews* v. *Rodgers*, 284 U.S. 521 (1932).

If the Court should accept jurisdiction over Arizona's complaint, New Mexico would move the Court to consider staying any further proceedings in this case until appeal of the state case to this Court has been perfected. Such action would be particularly appropriate in order to avoid duplicative effort in the two forums.

B. The Privileges And Immunities Clause Of Article IV And The Equal Protection Clause Of The Fourteenth Amendment Upon Which Arizona Relies May Be Invoked Only By Individual Citizens And Not By States. It Would Be Inappropriate To Grant Jurisdiction Over Arizona's Proprietary Claim Under The Commerce Clause Where All Arizona Utilities Are Already Litigating The Constitutionality Of The Tax And That Litigation Will Resolve The Issues Arizona Raises In the Complaint.

That this Court should not grant Arizona's motion is evident from *Massachusetts* v. *Missouri*, 308 U.S. 1, 17 (1939). There the Court refused to hear Massachusetts' attempt to enjoin Missouri from taxing property in trusts established by a decedent Massachusetts domiciliary, holding that original jurisdiction could not be invoked on behalf of its residents to challenge the imposition of taxes by Missouri. Here, too, if Arizona's citizens are denied equal protection and denied privileges and immunities accorded New Mexicans, they themselves may raise the claims. The constitutional guarantees of these two clauses extend to individuals and not to states. A state is not a "person" entitled to equal protection of the laws under the Fourteenth Amendment, *Wisconsin* v. *Zimmerman*, 205 F.Supp. 673 (W.D. Wis. 1962), *cf. South Carolina* v. *Katzenbach*, 383 U.S. 301, 323-24 (1966), nor a "citizen" entitled to the rights of the privileges and immunities clause. *Hague* v. *C.I.O.*, 307 U.S. 496, 514 (1939); *Paul* v. *Virginia*, 75 U.S. 168, 178-80 (1868). Indeed, it is noteworthy that *Austin* v. *New Hampshire*, 420 U.S. 656 (1975), upon which Arizona relies, was successfully pursued by individual taxpayers, as has every other challenge brought before the Court to the validity of a tax on privileges and immunities or equal protection grounds. See *e.g.*, *Wheeling Steel Corp.* v. *Glander*, 337 U.S. 562 (1949); *Toomer* v. *Witsell*, 334 U.S. 385 (1948); *Travis* v. *Yale & Towne Mfg. Co.*, 252 U.S. 60 (1920); *Travellers Insurance Co.* v. *Connecticut*, 185 U.S. 364 (1902); *Ward* v. *Maryland*, 79 U.S. (12 Wall) 418 (1870). Whatever the result might be of an individual action brought by an Arizona consumer it is clear that Arizona has no *parens patriae* cause of action on equal protection or privileges and immunities grounds.

As for its proprietary right of action, defendant submits that it should also not be heard by this Court. Arizona must, of course, represent an interest of her own and not merely that of her citizens or corporations. *Arkansas* v. *Texas*, 346 U.S. 368, 370 (1953). True, in *Pennsylvania* v. *West Virginia*, 262 U.S. 553 (1922), the Court did grant original jurisdiction over a commerce clause claim that a state was, by regulatory action against gas utilities, shutting off the supply of natural gas to neighboring states heavily dependent on the gas. But in this case New Mexico is not taking any action which will cut off or even reduce the flow of interstate commerce in electricity; it is merely taxing the generation of electricity, an activity which for over four decades has been held a local event that the states are free to tax. *Utah Light & Power Co.* v. *Pfost*, 286 U.S. 165 (1932). Moreover, Arizona's political subdivision, Salt River Project, is at present participating as a party plaintiff in a declaratory judgment action in New Mexico which will dispose of all the constitutional arguments Arizona asks to raise here. And as long as the New Mexico litigation lasts, the Arizona utilities will pay no generation tax, hence Arizona will not have to bear any increase in the price it pays for electricity. Thus, in view of the existence of that litigation Arizona will never be damaged by the tax, and the only substantial interest Arizona is advocating here is that of her utilities. We submit that this Court should not assume jurisdiction over so insubstantial a proprietary claim as Arizona's.

II. New Mexico's Electrical Energy Tax Neither Discriminates Unconstitutionally Against Interstate Commerce Nor Does It Burden Interstate Commerce.

A. New Mexico's Tax Structure Subjects The In-State Dispostion Of Electricity To A Greater Rate Of Taxation Than Electricity Generated For Sale Outside The State; Hence, Under Well-Established Precedents Of This Court The Act Does Not Discriminate Against Interstate Commerce.

The heart of plaintiff's argument is the foremost contention in its brief that New Mexico discriminates against the interstate commerce carried on by Arizona Public Service Co., Tucson Gas & Electric Co. and Salt River Project. These utilities generate electricity in New Mexico but sell it in Arizona.

Plaintiff's argument is simple: only those utilities generating electricity in New Mexico that sell the electricity in New Mexico are entitled to the gross receipts tax credit. This discriminates, plaintiff says, against Arizona utilities generating electricity in New Mexico. This contention is misconceived because it rests upon (1) a musunderstanding of the scope and operative effect of New Mexico's tax structure as to electricity; (2) the assumption that the Arizona utilities in generating electricity are engaged in interstate commerce; and (3) a reliance on cases of this Court which are not on point. Moreover, plaintiff fails to cite the cases which are controlling, the most important of which is *Public Utility District No. 2 of Grant County* v. *State of Washington*, 82 Wn.2d 232, 510 P.2d 206 (1973), appeal dismissed for want of a substantial federal question, 414 U.S. 1106 (1974). Others are *South Carolina Power Co.* v. *South Carolina Tax comm'n*, 52 F.2d 515 (E.D.S.C. 1931), aff'd 286 U.S. 525 (1932); *Hinson* v. *Lott*, 75 U.S. 148 (1869); *Gregg Dyeing* v. *Query*, 286 U.S. 472 (1931); *Henneford* v. *Silas Mason Co.*, 300 U.S. 577 (1937); *Southern Pacific Co.* v. *Gallagher*, 306 U.S. 167 (1939); *Doscher* v. *Query*, 21 F.2d 521 (E.D.S.C. 1927); and *Oldetyme Distillers, Inc.* v. *Gordy*, 17 F. Supp. 424 (D.Md. 1936). Furthermore, plaintiff fails to discuss or distinguish *Alaska* v. *Arctic Maid*, 366 U.S. 199 (1961), a case which squarely rejected the very contention plaintiff makes in this case.

The fundamental flaw in plaintiff's discrimination argument is that it is based on too narrow a view of the question. Plaintiff would look solely to the question of how the generator of electrical energy is taxed. In taking this narrow approach, it ignores two critical points. First, the practical operation and effect of a tax on the subject or article of commerce, *not the tax status of a particular taxpayer*, controls in determining whether a tax discriminates against interstate commerce under the Commerce Clause. There must be taken into account the impact of the total scheme of state taxation, rather than just the impact on a particular taxpayer.

Second, there is no discrimination against interstate commerce if the commodity of commerce, in this instance electricity, is subject to equivalent taxation by New Mexico. Receipts from sales of electrical energy at retail in New Mexico are taxed at the rate of 4 percent, the Electrical Energy Tax burden on Arizona utilities generating in New Mexico will never be greater than that. In fact, it will be substantially less. Thus, there is equivalence of taxation as is required under the cases discussed below.

These two points will be discussed in subsections 1 and 2 which follow.

1. The Tax Burden On A Particular Taxpayer Or Particular Taxable Incident Is Not Controlling. The Total Tax Structure Must Be Considered In Determining Whether An Unconstitutional Discrimination Exists.

We are not here concerned primarily with the impact of a particular tax on particular taxpayers. Rather, the basic inquiry must be whether or not New Mexico's total tax structure discriminates against interstate commerce. The correctness of this broad approach has been recognized by this Court in resolving the discrimination question in the early case of *Hinson* v. *Lott*, 75 U.S. 148 (1869), and the more recent use tax discrimination cases of *Henneford* v. *Silas Mason Co.*, 300 U.S. 577 (1937), *Southern Pacific Co.* v. *Gallagher*, 306 U.S. 167 (1939). It was also recognized by the Supreme Court of Washington and this Court in an electrical energy tax case so analogous to this case as to be dispositive of the issue here presented, *Public Utility District No. 2 of Grant County* v. *State*, 82 Wn.2d 232, 510 P.2d 206 (1973), appeal dismissed for want of a substantial federal question, 414 U.S. 1106 (1973).*

In the *Public Utility District No. 2* case, the Washington Supreme Court had before it a Washington tax on generation of electricity which allegedly discriminated against utilities that sold electricity out of state. Instead of a credit system like New Mexico's, Washington taxed the sale of power at every level of distribution, but allowed a *deduction* for receipts from resale of the power in-state. If the power was resold out-of-state, the deduction was not available. The utilities argued that the unlawful discrimination occurred because the wholesaler or generator who sold for resale in the state received the deduction, while the wholesaler or generator who sold to an Oregon utility for resale in Oregon did not. To this argument the Washington court responded:

> " . . . a proper analysis must take the whole scheme of taxation into account to determine whether the actual operation of that taxing structure in its relationship to intrastate and interstate commerce results in an unconstitutional discrimination against the latter. (Here the Court footnotes 12 U.S. Supreme Court and state court decisions.)

*The appeal to this Court was based on the contention that the Washington electrical energy tax discriminated against interstate commerce in violation of Article I, Sec. 8 of the United States Constitution. The dismissal by this Court means that the case was decided *on the merits* and that lower courts presented with the same issue are bound by the decision. *Hicks* v. *Miranda*, —U.S.—, 95 S.Ct.2281, 45 L.Ed. 223 (1975).

"*Considered in isolation*, as urged by respondents, the Washington tax deduction provision may also be discriminatory; it was intended to apply solely to sales for resale within this state. Alone, it may be invalid, but *it does not stand alone*, and this fact, and the failure of the respondents and the trial court below to so recognize, results in their abbreviated analysis. This isolated evaluation led the trial court in *Silas Mason Co.* v. *Henneford*, 15 F. Supp. 958 (E.D.Wash. 1936), rev'd, 300 U.S. 577, 57 S.Ct. 524, 81 L.Ed 814 (1937), to declare invalid the tax in question. Similarly, here, it could lead us to strike down the tax assessment without having correctly evaluated the taxing scheme's operation.

"This scheme contains no constitutional infirmity, for 'There is no demand in (the) Constitution that the state shall put its requirements in any one statute. It may distribute them as it sees fit, if the result, taken in its totality, is within the state's Constitutional power.' *Gregg Dyeing Co.* v. *Query*, 286 U.S. 472, 480, 52 S.Ct. 631, 634, 76 L.Ed. 1232 (1932). A similar deduction provision, RCW 82.03.430(6), was at issue in Crown Zellerbach in which a unanimous court found that to disallow the deduction ignores the lawful purpose behind its operation. Imposition of actual tax liability is the purpose advanced by such statutes in an effort to avoid double or triple tax liability as to particular products or activities. 'In other words, the policy is to impose *actual liability* for payment of tax only once . . .' *Crown Zellerbach Corp.* v. *State*, supra, 45 Wash. 2d at 753, 278 P. at 308." 510 P. 2d at 210 [Emphasis added.]

In *Hinson* v. *Lott*, *supra*, the combined effect of a distiller's (manufacturing) tax and a merchant's tax on the sale of imported liquor was considered. The merchant's tax was attacked on the ground that it discriminated against interstate commerce, by reason of the fact that it applied only to the sale of liquor imported into the state. This Court sustained the tax, holding that no discrimination existed, in view of the fact that locally proouced liquor, while not subject to the merchant's tax, was subject to the distiller's tax. These taxes were equivalent in amount but imposed on different taxpayers.

In the *Gallagher* and *Henneford* cases, this Court sustained use taxes imposed on products purchased without the state, holding that no discrimination existed in view of the fact that sales taxes were imposed on products sold within the state. This approach has been used to strike down, as well as sustain, state taxes. Thus, in *Halliburton Oil Well Cementing Co.* v. *Reily*, 373 U.S. 64 (1963), a use tax was found invalid as applied to an out-of-state fabricator using the fabricated goods in Louisiana, but this Court reaffirmed the broad approach of analyzing the entire tax structure. 373 U.S. 69-70.

These cases illustrate the proposition that it is the practical effect of the *total state tax burden* as applied to the commodity of commerce, here electrical energy, which ultimately controls.

2. The New Mexico Tax Structure With Respect To Electrical Energy Does Not Discriminate Against Interstate Commerce.

As clearly established by the cases discussed in the preceding subsection, the total tax burden imposed on different taxpayers or imposed on different aspects of one subject of taxation, here electricity, must be considered together in analyzing a claim of discrimination against interstate commerce. If the commodity of commerce (in *Hinson*, liquor, in *Southern Pacific Co.* v. *Gallagher* and *Henneford*, tangible personal property and in *Public Utility District No. 2* and in this case electrical energy) is subject to equivalent taxation by the state, whether ultimate use and consumption be within or outside this state, there is no discrimination.

The only basis for any discrimination argument is the credit against gross receipts tax allowed by Sec. 72-16A-16.1(B), N.M.S.A. 1953 (1975 Interim Supp.), the text of which was set forth previously in this brief. The obvious purpose of this provision is to collect a tax only once from in-state sellers, not to impose the generation tax in addition to the 4 percent gross receipts tax. The in-state sale of electricity generated in New Mexico is not exempted; it is taxed, just as the out-of-state electricity is, and at the significantly *higher* rate of 4 percent. The legislative purpose is no different from that found by the Washington Supreme Court in the case of *Public Utility District No. 2* v. *State*, *supra*, where it sustained a privilege tax on electricity so close to the tax at issue here as to the foreclose plaintiff's commerce clause contentions in this case.

The tax in *Public Utility District No. 2* v. *State* was a privilege tax on the light and power business measured by gross income. The tax was imposed at every level of distribution. The deduction which allegedly violated the commerce clause read as follows, 510 P.2d at 207, fn. 2:

"Deductions in computing tax. 'In computing tax there may be deducted from the gross income the following items: "'. . . (2) Amounts derived from the sale of commodities to persons in the same public service business as the seller, *for resale* as such *within this state* . . .'" [Emphasis added.]

The public utility districts sold power at wholesale to Washington utilities for resale in Washington. The income from these sales was deductible. They also sold at wholesale to Oregon utilities for resale in Oregon. The income from these sales was not deductible, producing the alleged discrimination. The Washington Supreme Court conceded that, viewed in isolation, the deduction provision could be discriminatory, but it went on to rule that the provision must also be considered in the light of the whole statutory framework for taxation of the subject matter:

"*The* public utility *tax on electrical power* originating in this state *is to be imposed only once* under the Washington taxing scheme. The deduction here at issue permits this singular tax imposition by preventing the pyramiding effect of the public utility tax, which is otherwise certain to occur. The only relevant difference between the present case and Crown Zellerbach is that, rather than having an interrelated tax structure (manufacturing-wholesaling) imposed, this case has a shifting tax structure in which singular tax liability exists but shifts to another utility. By so doing, the in-state distribution of the use of power is *not* exempted and is taxed, just as is the out-of-state distribution of power. Equal treatment is the theme of this system. *H & D Communications Corp.* v. *Richland*, 79 Wash. 2d 312, 484 P.2d 1141 (1971). The out-of-state utility is in no worse position than its instate competitor. The state is playing no favorite with its resident businesses at the expense of similarly situated out-of-state enterprises.

"The confusion results, in part, because the respondents look only to their status as complaining public utilities at the time of their sales to in-state or out-of-state purchasers, and not to the impact of the total tax structure on the subject matter here involved, the disposition and use of power. *If the whole tax scheme is evaluated, the tax deduction that is made at the sale to a Washington utility is made up at the time the Washington utility buyer sells to its customers.* Thus, 'In the instant case, there is no burden on interstate commerce that is not placed on intrastate commerce.' *H & B Communications Corp.* v. *Richland*, supra, 79 Wash.2d at 314, 484 P.2d at 1144. The in-state and out-of-state disposition of power is equally treated. There is tax equivalence here and no discrimination on interstate commerce.

"Judgment reversed." 510 P.2d at 211. (Emphasis added.)

Similarly, New Mexico's intention with respect to electrical energy generated and sold by utilities in New Mexico is that the transactions be taxed only once. Consequently, the legislature has provided that the electrical energy tax may be credited against the gross receipts tax due on subsequent sales in New Mexico. Obviously, the same result could have been accomplished by imposing the type of tax and deduction sustained in the Washington *Public Utility District No. 2* case. The tax effect is the same in both structures; the difference lies only in the form of the two systems, not in their substance.

There are a number of other precedents which strongly support the constitutionality of New Mexico's choice to allow the electrical energy tax credit against gross receipts tax. These cases consider not the impact of a particular tax on a particular taxpayers, but whether the total tax structure with respect to electrical energy discriminates against interstate commerce.

A South Carolina statute containing the credit feature of New Mexico's tax scheme was considered in *South Carolina Power Co.* v. *South Carolina Tax Commission*, 52 F.2d 515 (E.D.S.C. 1931), aff'd 286 U.S. 525 (1932). South Carolina imposed a tax of 5/10 of one mill upon each kilowatt hour of electric power *generated* in South Carolina and also an excise tax of 5/10 of one mill upon each kilowatt hour of electricity *sold* in the state. This statute provided that if the seller subject to the sales tax procured electric power which was subject to the payment of the privilege tax, a *credit* on the sales tax in the amount of the privilege tax already paid by the person generating the electricity would be allowed. Utilities attacked the South Carolina taxes as unconstitutionally burdening and discriminating against interstate commerce. In commenting upon this statutory scheme the court noted:

"The evident purpose of the act is to impose a tax upon the current used within the State and to impose it at the source or as soon as the current becomes subject to the jurisdiction of the taxing power, but not to impose but once . . . If current produced as well as sold within the state were subjected to the

sales tax such current would rest under a double burden of taxation. To avoid this and at the same time to preserve the system of taxing at the source, current which is produced within the state is taxed at the time of generation but is relieved of the sales tax, which is equal in amount, with the result that all currents sold within the state, whether produced there or brought in from another state, pays exactly the same tax." 52 F.2d at 521.

In resolving the question of validity of the tax on the generation of electrical current, the court upheld the tax on the basis of taxable events *preceding* interstate commerce on authority of *Oliver Iron Mining Co.* v. *Lord*, 262 U.S. 172 (1923), *Hope Natural Gas Co.* v. *Hall*, 274 U.S. 284 (1927) and *American Manufacturing Co.* v. *St. Louis*, 250 U.S. 459 (1919). In reference to current brought into the state which was subject to the sales tax the court said:

"The point that the tax on sales is a discrimination against current which has passed in interstate commerce, because current which has paid the local generation tax is exempted from the sales tax, has already been considered in discussing the points raised under the Fourteenth Amendment. The cases of Hinson v. Lott, supra, 8 Wall.148, 19 L.Ed. 387 and Doscher v. Query, supra (D.C.) 21 F. (2d) 521, 525, sufficiently answer this proposition." 52 F.2d at 526.

Citing the *South Carolina Power* and *Hinson* cases, *Oldetyme Distillers, Inc.* v. *Gordy*, 17 F.Supp. 424 (D.Md. 1936) also held that a whiskey manufacturing tax credit against a subsequent sales tax did not discriminate against interstate commerce.

The totality of a state's pattern of taxation was recognized by this Court in the license tax case of *Alaska* v. *Arctic Maid*, 366 U.S. 199 (1961). Alaska imposed a "license" tax upon only the business of operating freezer ships and other floating cold storages, measured by the value of fish obtained for processing through freezing. In fact, the tax fell only upon out-of-state businesses because they were the only ones who operated freezer ships. The ship operators purchased fish caught in Alaskan territorial waters, froze the fish and then transported the fish to the State of Washington for canning. They alleged that the Alaskan taxing scheme discriminated against their interstate businesses because (1) there was no tax on fish caught and frozen in Alaska and destined for canning in Alaska, and (2) fish processors selling fresh frozen fish in the Alaskan consumer market were taxed at a lower rate.

This Court first found that the license tax was imposed upon an occupation made up of local activities within the reach of Alaska's taxing authority, citing *Oliver Iron Mining* v. *Lord*, *supra*, and *Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 347 U.S. 157 (1954). It then held that the tax in question did not discriminate against interstate commerce because in-state businesses which had to Pay other local taxes rather than the license tax, were not preferred against out-of-state competitors. The Court reasoned that there could be no discriminatory preference in favor of local canners because they paid a greater tax upon fish obtained for canning. The Court stated:

"When we look at the tax laid on local canners and those laid on 'freezer ships' there is no discrimination in favor of the former and against the latter. For no matter how the tax on 'freezer ships' is conputed, it did not exceed the six per cent tax on the local canners. Hence cases such as Pennsylvania v. West Virginia (citation omitted) which hold invalid state laws that prefer local sales or interstate sales, are inapposite." 366 U.S. at 204-205.

In this case, the generation tax on electrical energy, no matter how it is computed, does not exceed the 4 percent burden on in-state disposition of power.

In *Gregg Dyeing Co.* v. *Query*, 286 U.S. 472 (1931), this Court upheld a complementary taxing statute imposed on gasoline brought into the state for storage, use and consumption against the contention that the statute discriminated against interstate commerce. In disposing of this argument, the Court construed a separate statute *in pari materia* and concluded it imposed an equivalent tax on use and consumption of gasoline in the state.

Henneford v. *Silas Mason Co.*, *supra*, *Southern Pacific Co.* v. *Gallagher*, *supra*, and *Hinson* v. *Lott*, *supra*, also support the proposition that New Mexico's generation tax and gross receipts tax credit work no discrimination against plaintiffs because the New Mexico burden on in-state disposition of electricity is greater than the generating tax on electricity taken out of New Mexico.

New Mexico's tax structure with respect to electricity is not distinguishable constitutionally from the electrical energy tax cases of *Public Utility District No. 2* and *South Carolina Power Co.*; the liquor cases of *Hinson* v. *Lott*, and *Oldetyme Distillers*; the sales and use tax cases of *Gallagher* and *Henneford* v. *Silas Mason Co.*; and the license tax case of *Arctic Maid*. These cases establish that the tax burden imposed on different taxpayers or imposed on different incidents of taxation must be considered together in resolving the discrimination issue. And they held that there is no discrimination

against interstate commerce if the commodity of commerce, here electrical energy, is subject to equivalent taxation by the state, whether or not the ultimate use and consumption is within or without the state.

The issue of discrimination against interstate commerce is a practical one, not an abstract or academic question. As stated by this Court in *McGoldrick* v. *Berwind-White Coal Mining Co.*, 309 U.S. 33, 45 fn. 2 (1940):

> "Despite mechanical or artificial distinctions sometimes taken between the taxes deemed permissible and those condemned, the decisions appear to be predicated on a practical judgment as to the likelihood of the tax being used to place interstate commerce at a competitive disadvantage." (Reference to numerous cases follows in the footnote.)

In the *Arctic Maid* case, the Court reasoned that there could be no such discriminatory competitive preference, since Alaskan processors freezing fish for the local retail market were not in competition with processors freezing fish for canning out of state. This was precisely the same reasoning approved by this Court in the *Public Utility District No. 2* case where it was held that there was no discriminatory preference for in-state business because:

> ". . . the public utility districts selling out-of-state are not in competition with one who sells in-state." 510 P.2d at 210.

Similarly, the Arizona utilities taxed under the Electrical Energy Tax Act are not in competition with New Mexico electrical utilities, and plaintiff does not allege that they are.

New Mexico seeks to tax the generation of electrical energy in this state. All generators of electrical energy in this state must pay the tax. That the electrical energy tax may be credited against gross receipts tax is only to prevent in-state power from being subjected to more than a 4 percent tax. It does not have the effect, under New Mexico's tax structure, of exempting the in-state generation and sale of power. This state's tax structure on electrical energy is designed to subject to one tax, but only one tax, the commodity of electrical energy. The taxation of this subject does not discriminate against interstate commerce.

In its complaint (second cause of action, Par.IV) and brief (pp. 21, 23, 26) Arizona makes much over its allegation that the New Mexico legislature intended to discriminate against Arizonans and interstate commerce. This allegation is reminiscent of the one made in *Heisler* v. *Thomas Colliery Co.*, 260 U.S. 245 (1922). There, plaintiffs claimed that the Governor of Pennsylvania advocated enactment of a tax on coal production because it would exact "tribute" from interstate commerce. This Court said, 260 U.S. 258-59:

> "The contention that the tax is a regulation of interstate commerce seems to be based somewhat upon the declaration of the Governor of the State of its effect upon consumers in other States. We are unable to discern in the fact any materiality or pertinency, nor in the fact that Pennsylvania has a monopoly (if we may use the word) of the coal. Whether any statute or action of a State impinges upon interstate commerce depends upon the statute or action, not upon what is said about it or the motive which impelled it . . ."

B. The Electrical Energy Tax Act Does Not Burden Interstate Commerce. The Generation Of Electricity Is A Local Activity Which New Mexico May Tax.

The question whether New Mexico's generation tax discriminates against the interstate commerce of the Arizona utilities because of the presence of the credit against gross receipts taxes has been answered by the ample precedents of this Court. Leaving the discrimination-credit question, we turn to the question whether the generation tax burdens interstate commerce. Here, too, the case law of this Court indicates that it does not. The tax is imposed upon the local activity of generation. The New Mexico legislature intended to tax "the privilege of generating electricity in this state for the purpose of sale;" this is not a tax on interstate commerce.

The following cases all support the proposition that the states may tax an intrastate activity such as the generation of electricity: *Utah Power & Light Co.* v. *Pfost*, 286 U.S. 165 (1932); *Oliver Iron Mining Co.* v. *Lord*, 262 U.S. 172 (1923); *Hope Natural Gas Co.* v. *Hall*, 274 U.S. 284 (1927); *American Manufacturing Co.* v. *St. Louis*, 250 U.S. 459 (1919); *Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 347 U.S. 157 (1954); *Heisler* v. *Thomas Colliery Co.*, 260 U.S. 245 (1922); and *Federal Power Commission* v. *Union Electric Co.*, 381 U.S. 90 (1964).

Utah Power & Light Co. v. *Pfost* is precisely on point. There the appellants generated electricity in intrastate commerce and also transmitted electricity in interstate commerce, just as the Arizona utilities involved in this case do. The activity of generation was taxed by Idaho under a statute indistinguishable from New Mexico's.

"any individual . . . engaged in the generation of . . . of . . . electrical energy . . . for . . . sale . . . shall . . . pay thereon a license tax of one-half mill per kilowatt hour . . ." 286 U.S. at 175.

The Court held that the tax did not, as to electricity transmitted outside the taxing state, impose an unconstitutional burden on interstate commerce. Just as Arizona contends here, Utah Power & Light Company argued that it was the interstate transmission which constituted the subject of taxation since the transmission could not be separated from the generation or production of electrical energy. In disposing of Utah Power's argument, this Court found that the generation or production of electrical energy is analogous to the manufacture of a more tangible product and concluded that the Idaho tax was imposed on a valid local privilege.

After analyzing the process by which electrical energy is created and transmitted, the Court concluded, 286 U.S. 181-82:

"We are satisfied, upon a consideration of the whole case, that the process of generation is as essentially local as though electrical energy were a physical thing; and to that situation we must apply, as controlling, the general rules that commerce does not begin until manufacture is finished, and hence the commerce clause of the Constitution does not prevent the state from exercising exclusive control over the manufacture. Cornell v. Coyne, 192 U.S. 418, 428, 429, 48 L.Ed. 504, 508, 509, 24 S.Ct. 383. 'Commerce succeeds to manufacture, and is not a part of it.' United States v. E. C. Knight Co., 156 U.S. 1, 12, 39 L.ed. 325, 329, 15 S.Ct. 249."

"Without regard to the apparent continuity of the movement, appellant, in effect, is engaged in two activities, not in one only. So far as it produces electrical energy in Idaho, its business is purely intrastate, subject to state taxation and control . . . The situation does not differ in principle from that considered by this court in Oliver Iron Min. Co. v. Lord, 262 U.S. 172, 67 L.ed. 929, 43 S.Ct. 526. There the State of Minnesota has imposed an occupation tax on the business of mining ores . . ."

Utah Power & Light remains good law. See, *e.g. Parker* v. *Brown*, 317 U.S. 341, 360 (1943); *Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 347 U.S. 157 (1954); *Federal Power Commission* v. *Union Electric Co.*, 381 U.S. 90 (1964).

In *Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, *supra*, the Court dealt with a tax on the activity of "gathering gas" as applied to an interstate pipeline company. It struck down the tax, holding that it was upon interstate commerce itself. The Court distinguished such a tax from valid taxes imposed upon local commerce before interstate commerce has begun, citing *Utah Power & Light Co.* v. *Pfost*, *supra; Hope Natural Gas Co.* v. *Hall*, *supra* (tax on production of gas is not violative of the commerce clause since production precedes interstate commerce); and *Oliver Iron Mining Co.* v. *Lord*, *supra* (mining of ore is local event, not part of interstate commerce, which state is free to tax). Two similar cases hold that manufacturing, *American Manufacturing Co.* v. *St. Louis*, *supra*, and mining of coal, *Heisler* v. *Thomas Colliery Co.*, *supra*, are all events preceding interstate commerce which the states may tax.

Under long-established cases of this Court, then, New Mexico's generation tax very clearly does not burden interstate commerce.

III. New Mexico's Electrical Energy Tax Structure Does Not Violate The Equal Protection Or Privileges And Immunities Clauses Of The United States Constitution.

Plaintiff contends that the New Mexico legislature has without reasonable basis classified Arizona utilities generating electricity, upon whom the legal incidence of the tax falls, differently from other taxpayers of the same class. However, Plaintiff fails to note that under both the equal protection and privileges and immunities clauses, the legislature has very broad power to classify for taxation purposes. In fact, there is a rational basis for distinguishing between generators of electricity who are subject to New Mexico gross receipts tax on the subsequent sale of the power and those who are not.

Concerning the power of state legislatures to classify for taxation purposes, the Court in *Madden* v. *Kentucky*, 309 U.S. 83, 88 (1940), said:

"This Court fifty years ago concluded that 'the Fourteenth Amendment was not intended to compel the State to adopt an iron rule of equal taxation,' and the passage of time has only served to underscore the wisdom of that recognition of the large area of discretion which is needed by a legislature in formulating sound tax policies. Traditionally, classification has been a device for fitting tax programs to local needs and usages in order to achieve an equitable distribution of the tax burden. It has, because of this, been pointed out that *in taxation, even more than in other fields, legislatures possess the greatest freedom in classification.* The burden is on the one attacking the legislative arrangement to negative

every conceivable basis which might support it." (Emphasis added; footnotes omitted.)

It then upheld a state's classification taxing deposits in banks outside the state at 50 cents per thousand and deposits in banks within the state at only 10 cents per thousand.

In *Lehnhausen* v. *Lake Shore Auto Parts Co.*, 410 U.S. 356 (1973), reh. den., 411 U.S. 910 (1973), the Court upheld a state *ad valorem* personal property tax imposed on corporations which was not imposed on individuals. The court there stated the equal protection test in the following language:

> "The Equal Protection Clause does not mean that a State may not draw lines that treat one class of individuals or entities differently from the others. The test is whether the difference is treatment is an invidious discrimination. Harper v. Virginia Board of Elections, 383 U.S. 663, 666. Where taxation is concerned and no specific federal right, apart from equal protection, is imperiled, (citing as an example a tax that discriminates against interstate commerce such as one on the "gathering of gas" shipped interstate, Michigan-Wisconsin Pipleine Co. v. Calvert, 347 U.S. 157 (1954) the States have large leeway in making classifications and drawing lines which in their judgment produce reasonable systems of taxation." 410 U.S. at 359.

Of course, as discussed in this brief, the generation tax is not a tax on interstate commerce, nor does New Mexico's tax structure discriminate against interstate commerce.

Allied Stores of Ohio v. *Bowers*, 358 U.S. 522, 528 (1959) laid down the following test:

> ". . . Similarly, it has long been settled that a classification, though discriminatory, is not arbitrary nor violative of the Equal Protection Clause of the Fourteenth Amendment if any state of facts reasonably can be conceived that would sustain it."

Thus, the only inquiry to be made is whether there is any reasonable basis for classifying or treating generators of electricity who do not sell that electricity in New Mexico any differently than generators who do.

Presumably, plaintiff says that the class for purposes of their argument consists of all generators of electricity. Only those who sell their electricity in New Mexico are entitled to credit electrical energy tax against gross receipts tax. This works an unconstitutional discrimination, it says, against generators who do not sell electricity in this state. In other words, it is the fact that the utilities in plaintiff's state are not New Mexico gross receipts taxpayers and have no gross receipts tax liability against which to credit electrical energy tax which produces the alleged invidious discrimination.

The rational basis for allowing the credit of electrical energy tax against gross receipts tax is the obvious legislative intent to tax the commodity of electricity, from generation to consumption, once and only once.

The precedents which uphold New Mexico's tax structure against the argument that it discriminates against interstate commerce have the same force for equal protection and privileges and immunities purposes. So long as the total tax burden on in-state generators and sellers of electricity is equal to or, as in this case greater than the burden on generators who sell outside the state, there is no unlawful discrimination against interstate commerce, and there can be no unlawful discrimination on equal protection or privileges and immunities grounds. As a class, then, the Arizona utilities whose interest plaintiff represents are treated equally, for their tax burden is no greater than the in-state taxpayer's burden. For example, Public Service Co. of New Mexico is subject to a 4 percent tax, which is a higher rate than any of the Arizona utilities will ever have to pay.

In *South Carolina Power Co.* v. *South Carolina Tax Commission*, 52 F.2d 515 (E.D.So.Car. 1931), aff'd 286 U.S. 525 (1932), which also involved an electricity generation tax credit against subsequent sales tax, the credit was attached as violative of the equal protection clause. The Court unequivocally rejected the utilities' contention:

> "It is argued that the sales tax . . . violates the equal protection clause of the Federal Constitution . . . because it exempts from the tax sales of current upon which the generation tax has already been paid. All current sold within the state, whether produced there or brought in from another state, pays exactly the same tax." 52 F.2d at 521.

Plaintiff cites *Austin* v. *New Hampshire*, 420 U.S. 656, 95 S.Ct. 1191 (1975) as "a case richly suggestive of the situation here confronted." (Br. 25) In fact the case is simply not apposite. In contrast to New Mexico's generation tax which applies to all taxpayers in a non-discriminatory manner,* under New Hampshire's commuter tax ". . . no resident of New Hampshire is taxed on his foreign income. Nor is the

*Even taking the electrical energy tax credit against gross receipts tax, New Mexico generators who sell their electricity in New Mexico are taxed at the rate of 4 percent.

domestic earned income of New Hampshire residents taxed. If effect, then, the State taxes only the income of nonresidents working in New Hampshire. . ." 95 S.Ct. 1193-94. Moreover, in *Austin* the nonresident taxpayers themselves were asserting their right to non-discriminatory treatment. Here Arizona purports to assert those personal rights on behalf of its citizens, for which the original jurisdiction of this Court is not intended. *Massachusetts* v. *Missouri*, 308 U.S. 1 (1939).

CONCLUSION

In view of the fact that litigation pending in the New Mexico courts, which will eventually find its way to this Court, will resolve each constitutional issue Arizona attempts to present here; the fact that Arizona's interest in striking down the tax at issue is remote; and, as we submit, the fact that New Mexico's tax structure as to electricity is clearly constitutional under the precedents of this Court, Arizona's motion for leave to file its complaint should be denied.

Respectfully submitted,

TONEY ANAYA,
Attorney General of New Mexico.

JAN UNNA,
Special Assistant Attorney General of New Mexico.

DANIEL FRIEDMAN,
Special Assistant Attorney General of New Mexico.

APPENDIX A

State of New Mexico, county of Santa Fe, in the District Court.

NO. 50245

Arizona Public Service Co., El Paso Electric Co., Salt River Project Agricultural Improvement and Power District, Southern California Edison Company, and Tucson Gas & Electric Company, Plaintiffs, vs. *Fred O'Cheskey, Commissioner of Revenue, Bureau of Revenue, and State of New Mexico*, Defendants.

COMPLAINT

Plaintiffs bring this action for declaratory judgment pursuant to the New Mexico Declaratory Judgment Act, Chapter 340, Laws 1975, with respect to the constitutionality and validity of the Electrical Energy Tax Act, Chapter 263, Laws 1975, and for their complaint herein, state:

1. Arizona Public Service Company, an Arizona corporation, generates, transmits, distributes and sells electrical energy within the State of Arizona, and is regulated as a public service corporation by the Arizona Corporation Commission.

2. El Paso Electric Company, a Texas corporation, generates, transmits, distributes and sells electrical energy within the States of New Mexico and Texas, and is regulated as a public utility in New Mexico by the New Mexico Public Service Commission and in Texas by the cities of El Paso, Van Horn, Anthony and Clint.

3. Salt River Project Agricultural Improvement and Power District (hereinafter "Salt River Project"), a political subdivision of the State of Arizona, operating a federal reclamation project pursuant to contracts with the Secretary of the Interior, generates, transmits, distributes and sells electrical energy within the State of Arizona.

4. Southern California Edison Company, a California corporation, generates, transmits, distributes and sells electrical energy within the State of California, and is regulated as a public utility by the California Public Utilities Commission.

5. Tucson Gas & Electric Company, an Arizona corporation, generates, transmits, distributes and sells electrical energy within the State of Arizona, and is regulated as a public service corporation by the Arizona Corporation Commission.

6. Fred O'Cheskey is Commissioner of the Bureau of Revenue of the State of New Mexico. The Bureau of Revenue is the agency of state government charged with the administration and enforcement of the Electrical Energy Tax Act.

7. The Four Corners Power Plant is an electrical generating station composed of five generating units and related facilities located on Indian lands leased from the

Navajo Nation under Leases dated December 1, 1960 and July 1, 1966, duly approved by the Navajo Tribal Council and the Acting Secretary of the Interior.

8. Arizona Public Service Company owns and operates generating units Nos. 1, 2 and 3 at the Four Corners Power Plant. Arizona Public Service Company, El Paso Electric Company, Public Service Company of New Mexico, Southern California Edison Company and Tucson Gas & Electric Company each owns an undivided interest in generating units Nos. 4 and 5 at the Four Corners Power Plant.

9. The San Juan Generating Station is an electrical generating station composed of two generating units (one operational and one under construction) and related facilities located in San Juan County, near Waterflow, New Mexico.

10. Public Service Company of New Mexico and Tucson Gas & Electric Company each owns an undivided one-half (½) interest in the San Juan Generating Station.

11. Certain of the plaintiffs (Arizona Public Service Company and El Paso Electric Company) sell electrical energy generated from the Four Corners Power Plant to a foreign country, Mexico.

12. As shown on the Map of Principal Transmission Lines annexed hereto as Exhibit "A", the electrical system of each plaintiff is directly interconnected with the system of each other plaintiff and with the electrical systems of Public Service Company of New Mexico, the U.S. Bureau of Reclamation, and Utah Power and Light Company. Southern California Edison Company's system is also directly connected with San Diego Gas & Electric Company, the Department of Water and Power, City of Los Angeles, the Pasadena Department of Water and Power, and Pacific Gas & Electric Company; its system is indirectly but substantially interconnected with the several Pacific Northwest systems and through them to other utility systems in the western United States. The interconnected transmission lines thus constitute an interstate grid encompassing the West.

13. As a consequence of the system interconnections described in the preceding paragraph, the demand for electricity in the major urban centers served by the plaintiffs in Arizona, southern California, and the El Paso area of West Texas determines in substantial degree the amount of electrical energy generated at generating stations located in New Mexico (as well as those in other states). The electrical energy generated in New Mexico in response to such demand to which each plaintiff is entitled from its generation facilities is instantaneously transmitted over existing transmission lines to that plaintiff's service area.

14. All of the plaintiff's above-described transactions in the generation and transmission of electrical energy at the Four Corners Power Plant and the San Juan Generating Station, and the distribution and sales of such electrical energy, are in the course of commerce among the States and the Navajo Tribe of Indians, except for the aforesaid sales of electrical energy to Mexico, certain relatively insignificant sales made by Arizona Public Service Company within New Mexico to Utah International Inc., for operation of the Navajo Mine which provides the fuel for the Four Corners Power Plant, and for certain sales by El Paso Electric Company within its service area in the State of New Mexico. All other sales or exchanges of electrical energy in New Mexico by any plaintiff are wholesale sales to other electric utility companies on the interconnected systems in interstate commerce under the exclusive jurisdiction of the Federal Power Commission. Such interstate sales give rise to no New Mexico gross receipts tax liability under the New Mexico Gross Receipts and Compensating Tax Act.

15. Each plaintiff pays income, ad valorem, franchise and other taxes imposed by the State of New Mexico or its political subdivisions on it and other taxpayers similarly situated, and income, ad valorem, sales and use (or their equivalent), franchise, excise and other taxes imposed by the state of its incorporation on it and other taxpayers similarly situated.

16. Section 3 of the Electrical Energy Tax Act, Chapter 263, Laws 1975 (hereinafter the "Act"), purports to impose on persons generating electricity a privilege tax of four-tenths of one mill "on each net kilowatt hour of electricity generated in New Mexico" for the purpose of sale.

17. Subsection 9B of the Act provides that the electrical energy tax paid on electricity generated and consumed in New Mexico may be credited against the gross receipts tax due New Mexico. No credits of any type are provided with respect to the electrical energy tax imposed upon electricity generated in New Mexico but transmitted and consumed outside New Mexico.

18. Subsection 9C of the Act directs that the credit for electrical energy tax paid on electricity generated and consumed in New Mexico shall be assigned to the person selling the electricity for consumption in New Mexico on which New Mexico gross receipts tax is due, and further requires the assignee of such credit to reimburse the assignor for the amount of the credit so assigned.

19. The practical operation and effect of Sections 3 and 9 of the Act is to tax the generation of electricity in New Mexico but shift the incidence of such tax to those who sell or consume that electricity outside New Mexico since the person generating and selling electricity for consumption in New Mexico receives either a credit (under Subsection 9B) against his gross receipts tax due New Mexico or a reimbursement (under Subsection 9C) in an amount equal to the electrical energy tax payable on such electricity.

20. Plaintiff's retail sales of electrical energy transmitted from generating facilities in New Mexico to plaintiff's respective service areas in Texas, Arizona and California are subject to certain taxes imposed by those states, or the political subdivisions thereof, or both. Such taxes are variously denominated as sales or other types of excise taxes, but are uniformly imposed upon, or passed on to consumers of electricity in those states.

21. There is no provision of law in Texas, Arizona or California whereby any of the plaintiffs are entitled to any credit, offset or rebate for the electrical energy tax imposed on them by New Mexico.

22. Public Service Company of New Mexico, an electric public utility regulated by the New Mexico Public Service Commission, with respect to its share of electrical energy generated at the Four Corners Power Plant and the San Juan Generating Station, will in practical effect sustain no additional tax burden under the Electrical Energy Tax Act due to the provisions of Subsections 9B and 9C of the Act permitting the amount of electrical energy tax paid to be assigned or credited against its gross receipts tax liability due the State of New Mexico.

23. El Paso Electric Company will in practical effect sustain no additional tax burden under the Electrical Energy Tax Act with respect to the electrical energy generated in New Mexico and sold by it to consumers in New Mexico due to the provisions of Subsections 9B and 9C of the Act allowing the electrical energy tax to be credited against its New Mexico gross receipts tax liability.

24. Plains Electric Generation and Transmission Cooperative, New Mexico corporation, generates electrical energy at its generating plant near Algodones, New Mexico, and transmits and sells electrical energy solely to New Mexico electric utilities which are its members; however, by reason of Subsections 9B and 9C of the Act, it will incur no additional tax burden due to the Electrical Energy Tax Act.

25. Plaintiffs are informed and believe, and therefore allege, that no additional tax liability under the Electrical Energy Tax Act is incurred by any other person (as defined in the Electrical Energy Tax Act) engaged in the same business as plaintiffs upon electrical energy generated and consumed in New Mexico, due to the availability of the crediting provisions provided for under Subsections 9B and 9C of the Act.

26. Plaintiffs are informed and believe, and therefore allege, that all, or virtually all, of the additional taxes claimed to be due under the Electrical Energy Tax Act after application of Subsections 9B and 9C of the Act, will be borne by those persons, including plaintiffs, engaged in the generation of electricity in New Mexico which is transmitted across and consumed outside the boundaries of the State of New Mexico.

27. Plaintiffs are informed and believe, and therefore allege, that the Act was enacted for the purpose of and the view to placing the exclusive burden of paying additional tax revenues to the State of New Mexico upon transactions in commerce among the several states and with the Indian Tribes.

28. The language of the Act, coupled with the practical application of the tax, constitutes a tax on the privilege of engaging in commerce among the several states.

29. Plaintiffs contend that the Act is unconstitutional and void for each and every one of the following reasons:

A. The Electrical Energy Tax Act violates the Commerce Clause of Article I, Section 8 of the Unites States Constitution by deliberately and invidiously discriminating against and imposing direct and multiple burdens upon each plaintiff's interstate commerce in the transmission and sale of electricity.

B. Application of the Electrical Energy Tax to those plaintiffs, measured by electricity generated in New Mexico for transmission and sale in interstate commerce, is arbitrary, capricious and unreasonable and denies to each plaintiff the equal protection of the law, and the rights, privileges and immunities enjoyed by other members of the class defined as persons generating electrical energy in New Mexico, in violation of Section 1 of the Fourteenth Amendment to the United States Constitution, and of Article II, Section 18, and Article IV, Section 26 of the New Mexico Constitution.

C. The Act deprives plaintiffs of property without due process of law in violation of Section 1 of the Fourteenth Amendment to the United States Constitution and Article II, Section 18 of the New Mexico Constitution.

D. The Act violates Article I, Section 8, Clause 3, and Article I, Section 10, Clause 2 of the United States Constitution.

30. Plaintiffs are informed and believe, and therefore allege, that defendants contend the Act is constitutional with respect to the matters set forth in paragraph No. 29 of this Complaint.

31. The plaintiffs, being persons whose rights, status or other legal relations are affected by the Act, request that the Court determine the questions of validity arising under the Act.

32. A genuine controversy exists between the plaintiffs and defendants with respect to the matters hereinbefore alleged; however, there is no controversy respecting the amount of the tax which would be payable by any plaintiff, if the Act is valid, nor with respect to the form or accuracy of any assessment of tax thereunder.

33. Due to the necessity to construe and apply provisions of the United States Constitution and the New Mexico Constitution in order to resolve the controversy between plaintiffs and defendants, plaintiffs have no other plain, speedy and adequate remedy.

34. All conditions precedent to the commencement and maintenance of this action have occurred or been met.

WHEREFORE, plaintiffs pray:

A. That this Court adjudge and declare the Electrical Energy Tax Act, Chapter 263, Laws 1975, to be unconstitutional and void.

B. That upon final hearing and determination the defendants be enjoined from enforcing the Electrical Energy Tax Act and plaintiffs have such other and further relief as may be proper in the premises.

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Rodey, Dickason, Sloan, Akin & Robb, William C. Schaab, 221 Central Avenue, N.W., Albuquerque, New Mexico 87103.

Snell & Wilmer, Bruce Norton, 3100 Valley Center, Phoenix, Arizona 85073.

Montgomery, Federici, Andrews, Hannahs & Buell, Fred C. Hannahs, 350 East Palace Avenue, Santa Fe, New Mexico 87501.

By Fred C. Hannahs, Attorneys for plaintiffs.

WHITE, KOCH, KELLY & McCARTHY, Ben J. Phillips, Post Office Box 787, Santa Fe, New Mexico 87501. Co-counsel for plaintiff, El Paso Electric Company.

APPENDIX B

State of New Mexico, county of Santa Fe, in the District Court

No. 50245

Arizona Public Service Company, et al, Plaintiffs, vs. *Fred O'Cheskey, et al.*, Defendants.

MOTION TO DISMISS

Pursuant to Rules 12(b)(1) and 12(b)(6) of the Rules of Civil Procedure, Defendants Fred O'Cheskey, the Bureau of Revenue and the State of New Mexico move the court to dismiss Plaintiffs' complaint on the grounds that:

1. This Court lacks jurisdiction over the subject matter of this action because of Sec. 72-13-36, N.M.S.A. 1953 which provides:

> No court of this state has jurisdiction to entertain any proceeding by a taxpayer in which he calls into question his liability for any tax on the application to him of any provision of the Tax Administration Act (72-13-13 to 72-13-92), except as a consequence of the appeal by him to the court of appeals from the action and order of the commissioner all as specified in Sec. 72-13-38, N.M.S.A. 1953 Comp., or except as a consequence of a claim for refund as specified in Sec. 72-13-40 N.M.S.A. 1953 Comp.

2. Inasmuch as the Electrical Energy Tax Act does not, as a matter of law, violate any of the federal or New Mexico constitutional provisions which plaintiffs allege it does, the complaint fails to state a claim upon which relief can be granted.

Defendants' reasons and legal precedents upon which this motion is based are set forth in the brief annexed hereto.

TONEY ANAYA,
Attorney General.
JAN UNNA,
Bureau of Revenue,
Assistant Attorney General.
DANIEL H. FRIEDMAN,
Bureau of Revenue,
Assistant Attorney General.

CERTIFICATE OF SERVICE

I certify that the foregoing Motion, together with the brief in support thereof, was served by mailing a copy to each opposing counsel of record this 10th day of November, 1975.

JAN UNNA,
Bureau of Revenue,
Assistant Attorney General.

Senator FANNIN. The next witness is Mr. E. E. Fournace, senior vice president of the Ohio Power Co. in Canton, Ohio.

I don't know whether I pronounced your name correctly or not, sir.

STATEMENT OF E. E. FOURNACE, SENIOR VICE PRESIDENT, OHIO POWER CO., CANTON, OHIO

Mr. FOURNACE. You did very well, Senator Fannin. Thank you.

Senator FANNIN. You have a witness statement, do you, sir?

Mr. FOURNACE. I have a statement here. It will take me 5 minutes and I have copies for you.

Senator FANNIN. You may proceed as you desire.

Mr. FOURNACE. Thank you.

My name is Ebert E. Fournace. I am a vice president of Ohio Power Co., an electric utility operating company which serves approximately 585,000 customers in the State of Ohio.

I am appearing to urge the passage of S. 1957, which would prohibit any State or political subdivision thereof from imposing or assessing a tax on the generation of electricity which is transmitted and consumed outside such State.

Enactment of this bill is needed to stop the effort of certain States to impose on electric utilities quite substantial unapportioned taxes on exported electric energy, taxes which must in the final analysis be paid by the utilities' customers located in other States.

It has become increasingly common for electric utility customers to be served in part with electricity generated outside the State in which they reside.

The location of generating stations is influenced by a combination of factors, including, in the case of coal-fired plants, the availability of a nearby supply of coal so as to reduce the cost of transporting the coal, and the availability of an adequate supply of water.

Keeping generating costs as low as possible often dictates locating plants in States where some or all of the utilities' customers do not reside.

For these reasons, Ohio Power owns all or part of several generating stations in West Virginia, located mainly right on the Ohio River.

West Virginia has long had a "manufacturing" or production tax imposed on persons generating in West Virginia electricity which is delivered and sold in other States.

Ohio Power pays this tax which is now at a rate of 0.88 percent, or 88 cents per $100 valuation, of the value of the energy, on all its West Virginia generation.

A bill, S.B. No. 572, is pending in the West Virginia Legislature, however, to more than triple the tax rate, to 3 percent.

Ohio Power's revenue from electricity generated in West Virginia and sold in Ohio is subject to a 4 percent Ohio gross receipts tax. There is no credit against this Ohio tax for any tax paid to any other State with respect to this electric energy.

Parenthetically, I would like to say that Ohio's gross receipts tax does not apply to energy sold out of the State of Ohio, energy sold for resale, or to the Federal Government.

A State production tax on electric energy exported from the State of generation, such as the West Virginia tax I have described, is an unapportioned tax whose entire amount becomes added to the taxes imposed by the state in which the customers are located.

Under the systems of accounts prescribed for utilities by regulatory commissions, taxes are an operating expense, to be covered in the rates which the company charges its customers.

The rates for electricity moving in interstate commerce are thus burdened with the cost of the production tax of the State in which the electricity is generated.

The conceded purpose of increasing the rate of the West Virginia tax on exported electric energy is to shift tax burden from West Virginia consumers to out-of-State consumers, so that rates for electricity sold to West Virginia residents may be lowered; the increase in the tax rate on exported energy would be accompanied by a decrease in the tax rate levied on electricity sold in West Virginia.

It is the intention, and would be the effect, that the burden of the increased tax on exported electricity would be borne by out-of-State consumers.

Structuring State taxes so as to place an unapportioned burden on individuals and businesses located in other States invites retaliation.

It is very different from apportioning a tax, as happens with the net income tax on businesses, so that the tax is allocated among States on the basis of the various activities involved, such as selling in one State articles manufactured in another State.

Except for such taxes as property taxes and sales and use taxes, the practice has been, generally speaking, to impose taxes on electric utilities in the State in which the electricity is sold and the customer is located.

Such a tax commonly, although not universally, takes the form of a gross receipts tax levied by the State in which the electricity is sold on the revenues derived from the sale.

This is the Ohio structure. West Virginia also imposes a gross income tax on the revenues from sales to customers in that State.

Production taxes on exported energy should not be among those imposed by the State of generation.

A tax on the generation of electricity should not be compared with a severance or production tax on natural resources, such as oil, gas, mineral ores or coal. These are depletable, nonrenewable natural resources.

Electric energy, on the other hand, is not a natural resource. It is produced through the conversion of other energy into electricity.

The fuel for Ohio Power's West Virginia generating stations is coal, and the coal is West Virginia coal. While the generation process uses West Virginia coal, a depletable natural resource of that State, a tax is borne by the utility for consuming this resource.

West Virginia imposes a tax on the severance or production of coal at the rate of 3.85 percent of the value of the coal produced.

The State in which the exported electric energy is produced derives a number of economic benefits from such generation; it should not have the added benefit of an export tax at the expense of out-of-State consumers.

Most modern generating units are big, and their very high costs include large amounts for construction labor over a period of several years, providing many jobs, largely for residents of the locality, during the construction period.

Some of the materials which go into the construction are purchased locally. Significant employment is provided to operate and maintain the station after it goes into service, and there is, of course, other stimulus to the local economy.

The coal necessary to fuel powerplants is often mined in the State of generation, providing employment and other economic benefits from mining the coal.

Generating stations also provide large tax revenues for the State and its local subdivisions over the life of the plant, notably in the form of property taxes, which are very substantial because of the huge investment in such plants.

S. 1957 should be enacted into law to prohibit the imposition of State or local taxes on the generation of electric energy which crosses state lines and is consumed in States other than the State of generation, in order to prevent these unapportioned taxes from placing an increasing burden on interstate commerce and to put an end to the shifting of tax cost from residents of the State of generation to individuals and businesses located in other States, who must already bear the cost of taxes imposed on their supplying utility by the States and localities of their residence.

Senator FANNIN. Thank you.

Mr. FOURNACE. Senator, I thank you for this opportunity.

Senator FANNIN. Thank you, Mr. Fournace. That was an excellent statement. I think you have covered the questions that we have asked regarding the equity of the general type of tax that is applied as compared with the tax on electricity.

We have said that should not be compared with a severance or production tax on natural resources such as oil, gas, minerals and coal because these are depletable, non-renewable natural resources.

Electrical energy, on the other hand, is not a natural resource. So, I think you have well brought out what we were discussing with the previous witness. You cannot compare this with the normal tax placed on commodities.

Mr. FOURNACE. That is correct.

Senator FANNIN. I appreciate your comments on that. The witnesses from the Southwest have stated that many new facilities are constructed on a joint-venture basis involving utilities from more than one state.

Is this same arrangement true in the eastern part of the country?

Mr. FOURNACE. It certainly is and will continue becuase of the necessity to have large units to gain the benefit of the economy of scale.

It also is a matter of financing, it is a matter of having the market.

Senator FANNIN. So, perhaps West Virginia, because they have the coal resource and all, will expand their facilities.

Mr. FOURNACE. That is correct. They were very anxious to have these stations built in West Virginia because of their industrial development programs. They had the coal, they had the water, and——

Senator FANNIN. What effect did it have on the planning and development of such facilities we were talking about?

Mr. FOURNACE. I am quite certain that nobody is going to consider putting facilities in a state where they are going to have taxation on generation.

Senator FANNIN. There is no way of knowing, just like the previous witness said about the tax in New Mexico, they need some money; the need for funds exists in every State of the United States.

Certainly, the U.S. Government needs a tremendous amount of money to cover their obligations, but if we all decide we are going to assess just on the basis of need and we are going to see that a burden is placed on someone else other than our own people, we are going to have turmoil in this country; are we not?

Mr. FOURNACE. Right.

Certainly I think that is true. In my lifetime, Senator, I have never known a time when a political subdivision or Federal Government didn't need more funds and I never knew a tax that was a temporary tax.

Senator FANNIN. I agree with you.

The temporary tax—the income tax used to be temporary.

Mr. FOURNACE. The gross receipts tax on electrical energy was passed in 1932 and 1933 in the midst of the depression in order to help people feed themselves, welfare.

It started out at 0.35 percent; it is now 4 percent. We have long passed that depression.

Senator FANNIN. I hope.

Well, thank you very much. I appreciate very much your testimony and it is good to have you here with us today.

Mr. FOURNACE. Thank you.

Senator FANNIN. The next witness is Mr. Richard L. Dailey, West Virginia State tax commissioner, Charleston, W. Va.

STATEMENT OF RICHARD L. DAILEY, TAX COMMISSIONER, STATE OF WEST VIRGINIA

Senator FANNIN. We welcome you here today, Mr. Dailey.

Mr. DAILEY. Thank you, Mr. Chairman.

I appreciate the opportunity and the State of West Virginia appreciates the opportunity to appear.

We have prepared a written statement together with an outline and a brief connected thereto.

Senator FANNIN. Fine.

Mr. DAILEY. We do wish to express our sincere appreciation to Mr. Morris of the Senate Finance Staff for providing us helpful information in relation to this hearing.

West Virginia strongly opposes S. 1957 in its present form, both as to the prohibition of taxation of generated electricity and its possible far-reaching effects into the areas of energy production and interstate taxation.

S. 1957 finds that generation of electricity from one State to another is an integral part of interstate commerce and, therefore, any privilege tax thereon is an unreasonable burden on interstate commerce.

Therefore, no State has the right to tax the same if produced within, but transmitted without. The conclusion that both the generation and transmission of electricity is an integral part of interstate commerce and thus is a burden thereon, is contra to the judicial findings by various State supreme courts and the U.S. Supreme Court.

It has been made quite clear that the generation or manufacture of electricity is a separate and distinct activity of local incidence subject to the control of the States including the taxing powers of the respective States.

To hold otherwise would be to say in a much broader scope that interstate commerce begins before the manufacture starts or is completed and thus, any activity of that nature if taxed would be a burden on interstate commerce.

There is a clear distinction on the manufacture or generation of electricity as opposed to its transmission or delivery.

Just as it is clear that the generation or manufacture of electricity should be taxed at the place of local incidence, it is equally as clear that the transmission and delivery in interstate commerce cannot be specifically taxed.

Generation and transmission of electrical power may be integral parts of the utility business, but clearly are not integral parts of interstate commerce, according to any burden test.

The manufacture, transportation and sale of any product is an integral part of that business, but not of interstate commerce according to the burden on interstate commerce test.

It was and is not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing business. Interstate businesses must pay their own way, too.

The question rather becomes—is the State exacting a constitutionally fair demand for the aspect of interstate commerce to which it bears a special relation?

In other words, has the State exerted its power in proper proportion to the taxpayer's activity within the State and to the taxpayer's consequent enjoyment of the opportunities, resources and protection which the State has afforded.

Specifically, it can be argued cogently that electric power companies located in West Virginia receive not only the ordinary and customary benefits of protection from government and the opportunity to seek redress in the judicial system, but they also benefit from the excellent natural resources in West Virginia in the form of coal, gas, timber, stone, oil and waterways.

These utilities consume the abundant natural resources of West Virginia. Should not they be asked to give something back in return to the State of West Virginia?

The U.S. Supreme Court and the West Virginia Supreme Court answered this question with a resounding yes.

Senate 1957 would weaken and thus give rise to substantial litigation via the interstate commerce question as it relates to State taxation by this probably weakening of the analytical tests established by the U.S. Supreme Court over the past 40 years, and used thusly in determining the validity of and principles of State taxation.

The generation of electric power is closely related to West Virginia, or any State, and there is a definite link, or connection between the State and the subject of the tax.

The multiple burden test would be emasculated by Senate 1957. No other State can tax the manufacture of the electricity in West Virginia, since it can only occur in West Virginia. Thus, it is not a tax on interstate commerce, but on conducting a business within the State of West Virginia.

Specifically, this bill relates to West Virginia in the following obtrusive manner:

1. Overturn the VEPCO case as decided by our State supreme court, and certiorari denied by the U.S. Supreme Court 416 U.S. 916, April 1, 1974, which decision—which is good law—allowed West Virginia to tax the manufacture of electricity at its point of manufacture for that value, while prohibiting the taxation of transmission or delivery of that particular electrical energy outside the State of West Virginia.

2. Provides a business tax-free haven for several energy manufacturers and discriminates against West Virginia manufacturers.

Over 70 percent of all energy manufactured in West Virginia is transmitted without our State.

If there is no tax on out-of-State generation, will the companies transmit more than 70 percent out of State?

There is presently transmitted 32,420,398,800 kwh without the State of West Virginia with a gross manufacturing value of over $½ billion. Should not West Virginia have the right to exact its fair share?

That manufactured electricity is taxed at 88 cents per hundred dollar value. Electricity manufactured that is destined for West Virginia residential and commercial users is taxed at $5.72 per $100 and $4.29 per $100 gross income respectively—who is presently being discriminated against? The answer is the West Virginian.

Additionally, those electric companies that transmit out-of-State in West Virginia and pay the manufacturing rate have available the "West Virginia Industrial Tax Credit" peculiar only to West Virginia, which effectively enables out-of-State transmitters of electrical energy to wipe out 50 percent of the business taxes otherwise owed to the State of West Virginia per taxable year.

Thus, allowing them in calendar year 1975 to effectively pay only 11 percent of the total business taxes paid to West Virginia by all electrical energy producers and providers.

More explicitly, with the West Virginia credit a company which solely or primarily transmits without West Virginia can pay as low as 7.69 percent of taxes paid by other manufacturers of energy or without the credit only as high as 20.51 percent of taxes paid by others.

Ohio Power, who testified here today, serving no one in West Virginia, pays only 50 percent of the taxes paid by other West Virginia manufacturers today and even less than other energy manufacturers.

Under Senate bill 1957, Ohio Power would pay no business taxes while enjoying the protection and services of our great State.

In this regard, it should be noted that perhaps this amendment to Public Law 86-272 is an overreaction to deal with a specific situation existing between two great States.

But this attempt to alleviate the problem between those States may in many other States—in West Virginia it will, unintentionally we hope, prohibit those States from exacting their fair share of taxes commensurate with the governmental services and protection provided together with the depletion of their natural resources as well as energy production capability.

In West Virginia, the business and occupation tax is our largest revenue producer. This bill as contemplated by Congress, S. 1957, would obviously result in a drop in State revenues.

In a time when the public is demanding more and better services from government, the only alternatives are:

1. Increase taxes to pay for these services, or:
2. Cut back these governmental services.

This latter means fewer highways, hospitals, and schools, and spending less for education.

If the choice is to keep government services where they are or increase them, the revenue loss that we would experience must be made up by increasing our personal income tax, the consumers sales tax, or the property tax, or the excise taxes in West Virginia. Possibly, there would be a return to more regressive taxes like the property tax and consumers sales tax.

With West Virginia's abundant natural resources being used in the production of electricity, it seems unconscionable that the State cannot ask for something in return for consuming those valuable resources.

Is it fair to ask West Virginians to subsidize the production of electricity used in other States in the form of higher taxes on ourselves and a continued loss of our natural resources without a just return?

We believe that there should not be discrimination among businesses either in intrastate or interstate commerce.

However, we also don't believe in favoritism legislation specifically for one segment of any industry or for several members of that industry, particularly at other's expense.

Senate 1957 is totally discriminating against those energy producers and providers who serve the citizenry within its own borders, in relation to West Virginia's situation.

We urge this subcommittee not to adopt Senate bill 1957 in its present form.

Transmission and delivery should not be taxed because that is a burden on interstate commerce—but, that is the judicial law today.

If the New Mexico and Arizona situation effectively skirts that established law, after a court decision, then deal with it, but properly using restricted language.

Don't place West Virginia and other States in a position of losing substantial revenues and, more importantly, creating a tax haven for Ohio Power, VEPCO, West Penn and Duquesne at the expense of all other West Virginia manufacturers and our citizens.

Thank you, sir.

Senator FANNIN. Mr. Dailey, are you saying that the tax charged the utilities and all is not passed on to the consumers outside your State?

Mr. DAILEY. I am sure it probably is.

Senator FANNIN. So, they do pay; in other words, they absorb the expenses of generating the power whether it is in a facility at cost or whatever it might be, however costs are effected; is that right?

Mr. DAILEY. I would assume all consumers absorb the cost that goes into building the rate structure.

Senator FANNIN. I asked Mr. O'Cheskey, and I will ask you: Does West Virginia have any concern for the possible retaliatory actions other States might take in light of the dramatic increase in this tax recently considered by your legislature?

Mr. DAILEY. First of all, Senator, what we (West Virginia) are talking about in electric generation is a tax which has been on our code books for a long time. What the other gentleman was discussing is certain developments in our State legislature today which is a result of an election year and the more recent high cost of electrical power.

We have advised the Governor that the bill in its lastest form is probably unconstitutional. So, you have nothing but rhetoric, and I do not expect to see that bill pass.

We do have concern that if we would do something that would create a situation where we would be taxing that power which is transmitted outside the State of West Virginia higher than that which remains within West Virginia, then there could be some retaliatory moves by others.

I have pointed out previously it is taxed much lower, that which goes out, rather than that which is taxed within.

Senator FANNIN. You heard the testimony. What effect do you think this would have on the construction of facilities intended to serve States outside of your areas?

Mr. DAILEY. Our tax has been in effect on Ohio Power and Appalachian Power and VEPCO when they built their facilities.

Senator FANNIN. Now they are seeing the chance of raising the tax on it, at least it seems to be a political game, but nevertheless it would be of serious consequences to those purchasing power outside of West Virginia.

Wouldn't this result in the restriction of any additional facilities within the State of West Virginia?

Mr. DAILEY. I assume if we took the position that there would be fantastic increases in the tax, certainly it would bear on their economic decision as to whether to provide future plants in West Virginia.

Senator FANNIN. Is it correct that you have some reservation about a taxing scheme which permits instate taxpayers to be free of a levy which is imposed on out-of-State taxpayers?

Mr. DAILEY. That is not the situation in West Virginia, sir.

Senator FANNIN. I know, but I am asking if you have some reservations about that.

Mr. DAILEY. I think there would be some reservations in how the language would be drafted.

Senator FANNIN. I am referring to other States that are involved, too.

Now, you mentioned something about in its present form you would oppose S. 1957.

Would you support it or perhaps would you think it would be fair and equitable in a different structure?

Mr. DAILEY. I think as long as that power, Senator, which can be transported without the State would not be taxed differently from that which remains within the State, as Senator Gravel mentioned at the beginning of the hearing, I think we could support that concept.

Senator FANNIN. Now, I am wondering, in your statement are you saying that the U.S. Supreme Court's denying certiorari is an affirmation of the constitutionality of West Virginia's tax?

Mr. DAILEY. I would also refer you to Utah Light and Power, sir, insofar as the State of West Virginia's ability to tax.

Senator FANNIN. Does that really mean anything in the strict legal sense?

Mr. DAILEY. Well, it was not decided on the merits by the United States Supreme Court. That would be a correct statement.

Senator FANNIN. So, it really isn't——

Mr. DAILEY. It means—well, we don't——

Senator FANNIN. In the strict legal sense.

Mr. DAILEY. In the strict legal sense, we don't know what the Supreme Court decided to do in denying certiorari.

Senator FANNIN. But in doing that it does not mean they have taken a position?

Mr. DAILEY. I think they had already taken a position in Utah Power and Light where——

Senator FANNIN. But in denying certiorari——

Mr. DAILEY. They didn't take a merit position on West Virginia versus VEPCO as such.

Senator FANNIN. Thank you, Mr. Dailey, very much.

I appreciate your being here and we appreciate your testimony.

Mr. DAILEY. Thank you for your time, sir.

[The prepared Statement of Mr. Dailey follows:]

PREPARED STATEMENT OF RICHARD L. DAILEY, STATE TAX COMMISSIONER, STATE OF WEST VIRGINIA

The State of West Virginia appreciates the opportunity to appear before the Subcommittee on Energy of the Senate Finance Committee and further wishes to express our sincere appreciation for the helpful aide supplied by Mr. Morris of the staff for information relating to Senate 1957 and this public hearing. West Virginia must strongly oppose Senate Bill 1957 in its present form, both as to the prohibition of taxation of generated electricity and its possible far-reaching effects into the areas of energy production and interstate taxation. S. B. 1957 finds that:

1. Generation and transmission of electricity from one state to another are integral parts of interstate commerce.
2. Any privilege tax thereon is an unreasonable burden on interstate commerce.
3. Therefore, no state has the right to tax the same if produced within but transmitted without.

Let us analyze those findings:

The conclusion that both the generation and transmission of electricity is an integral part of interstate commerce and thus is a burden thereon, is contra to the judicial findings by various state supreme courts and the U.S. Supreme Court.

It has been made quite clear that the generation or manufacture of electricity is a separate and distinct activity of local incidence subject to the control of the states including the taxing powers of the respective states.

To hold otherwise would be to say in a much broader scope that interstate commerce begins before the manufacture starts or is completed and thus any activity of that nature if taxed would be a burden on interstate commerce.

There is a clear distinction on the manufacture or generation of electricity as opposed to its transmission or delivery. Just as it is clear that the generation or manufacture of electricity should be taxed at the place of local incidence, it is equally as clear that that transmission and delivery in interstate commerce cannot be specifically taxed.

Generation and transmission of electrical power may be integral parts of the utility business, but clearly are not integral parts of interstate commerce, according to any burden test. The manufacture, transportation and sale of any product is an integral part of that business but not of interstate commerce according to the burden on interstate commerce test.

It was and is not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing business. Interstate business must pay its way.

The question rather becomes—is the state exacting a constitutionally fair demand for the aspect of interstate commerce to which it bears a special relation. In other words, has the state exerted its power in proper proportion to the taxpayer's activity within the state and to the taxpayer's consequent enjoyment of the opportunities, resources and protection which the state has afforded.

Specifically, it can be argued cogently that electric power companies located in West Virginia receive not only the ordinary and customary benefits of police and fire protection from government and the opportunity to seek redress in the judicial system, but they also benefit from the excellent natural resources in West Virginia in the form of coal, gas, timber, stone, oil and waterways. These utilities consume the abundant natural resources of West Virginia. Should not they be asked to give something back in return to the State of West Virginia? The United States Supreme Court and the West Virginia Supreme Court have answered this question with a resounding—YES.

Senate Bill 1957 would weaken and thus give rise to substantial litigation via the interstate commerce question as it relates to state taxation by this probable weakening of the analytical tests established by the U. S. Supreme Court over the past forty years, and used thusly in determining the validity and principles of state taxation.

The generation of electric power is closely related to the state and there is a definite link, or connection between the state and the subject of the tax.

The multiple burden test would be emasculated by Senate Bill 1957. No other state can tax the manufacture of the electricity in West Virginia since it can only occur in West Virginia. Thus it is not a tax on interstate commerce but on conducting a business within the State of West Virginia.

Specifically, this bill relates to West Virginia in the following obtrusive manner:

1. Overturn the VEPCO case as decided by our State Supreme Court, and certiorari denied by the U. S. Supreme Court 416 U. S. 916 (April 1, 1974) which decision allowed West Virginia *to tax the manufacture of electricity at its point of manufacture for that value while prohibiting the taxation of transmission or delivery outside the State of West Virginia.*

2. Provides a business tax-free haven for several energy manufacturers and discriminates against West Virginia manufacturers.

Over 70 percent of all energy manufactured in West Virginia is transmitted without our state.

If there is no tax will the companies transmit more than 70 percent out-of-state? There is presently transmitted 32,420,398,800 kwh without the State of West Virginia with a gross manufacturing value of $535,000,000. Should not West Virginia have the right to exact its fair share?—YES.

That manufactured electricity is taxed at .88 cents per hundred dollar value. Electricity manufactured that is destined for West Virginia residential and commercial users is taxed at $5.72/100 and $4.29/100 gross income respectively—who is presently being discriminated against?—The West Virginian.

Additionally those companies that transmit out-of-state in West Virginia and pay the manufacturing rate have available the West Virginia industrial tax credit peculiar only to West Virginia which effectively enables out-of-state transmitters of electrical energy to wipe out 50 percent of the business taxes per year.

Thus, allowing them in calender year 1975 to effectively pay only 11 percent of the total business taxes paid to West Virginia by electrical energy producers and providers. More explicitly with the West Virginia credit a company which solely or primarily transmits without West Virginia can pay as low as 7.69 percent of other manufacturers of energy or without the credit only as high as 20.51 percent.

Ohio Power—serving no one in West Virginia, pays only 50 percent of taxes of other West Virginia manufacturers today and even less than other energy manufacturers. Under Senate Bill 1957—no business taxes while enjoying the protection and services of our great state.

In this regard, it should be noted that perhaps this amendment to Public Law 86-272 is an overreaction to deal with a specific situation existing between two great states. But this attempt to alleviate the problem between those two great states may in many other states, in West Virginia it will, unintentionally (we hope) prohibit those states from exacting their fair share of taxes commensurate with the governmental services and protection provided together with the depletion of their natural resources as well as energy production capability.

In West Virginia, the business and occupation tax is our largest revenue producer. This law as contemplated by Congress would obviously result in a drop in state revenues. If, in a time when the public is demanding more and better services from government, the only alternatives are: (1) increase taxes to pay for these services, or (2) cut back these governmental services. This means building fewer highways, hospitals, and schools, and spending less for education. If the choice is to keep government services where they are or increase them, the revenue loss must be made up by increasing our personal income tax, the consumers sales tax, or the property tax, or the excise taxes in West Virginia. Possibly, there would be a return to more regressive taxes like the property and consumers sales taxes.

With West Virginia's abundant natural resources being used in the production of electricity, it seems unconscionable that the state cannot ask for something in return for consuming those valuable resources. Is it fair to ask West Virginians to subsidize the production of electricity used in other states in the form of higher taxes on ourselves and a continued loss of our natural resources.

Another important consideration may be the effect of this law on our federal system of government. Would not the Congress be placed in the position of taking away the state's power to tax a privilege occurring absolutely within its own borders? By depriving the State of West Virginia of its right to tax a local privilege occurring within its jurisdiction, Congress has removed a substantial portion of the state's taxing power. By removing the power to tax, the federal government may take away the state's power to create, not only a strong state government, but viable programs to deal with the problems facing America in its third century.

We believe that there should not be discrimination among businesses either in intrastate or interstate commerce. However, we also don't believe in favoritism legislation specifically for one segment of any industry or for several members of that industry.

Senate 1957 is totally discriminating against those energy producers and providers who serve the citizenry within its own borders.

We urge this subcommittee not to adopt Senate 1957 in its present form. Transmission and delivery should not be taxed because that is a burden on interstate commerce—but, that is the Judicial Law today. If the New Mexico and Arizona situation effectively skirts that established law, then deal with it, but properly in restricted language but don't place West Virginia and other states in a position of losing substantial revenues and more importantly creating a haven for Ohio Power, VEPCO, West Penn and Duquesne at the expense of all other West Virginia manufacturers and our citizens.

STATE OF WEST VIRGINIA POSITION STATEMENT ON S. 1957 BILL, TO AMEND THE ACT OF SEPTEMBER 14, 1959 (PUBLIC LAW 86-272; 73 STAT. 555)

INTERPRETATION AND ANALYSIS OF SEANTE BILL 1957

A breakdown of Senate Bill 1957 indicates there are three basic parts or premises upon which the bill is predicated. The first part of the legislation states that Congress finds the generation and transmission of electricity from one state to another are integral parts of interstate commerce.

The second part states that any privilege tax on the generation and transmission of electricity from one state to another is an unreasonable burden on interstate commerce.

The third part states that no state has the power to tax the privilege of conducting interstate commerce activity, if the tax is on the generation of electricity within a state, which is then transmitted without the state.

A part-by-part analysis of the bill reveals the following. First, the bill would have Congress state a conclusion that the generation and transmission of electricity from one state to another is an integral part of interstate commerce. This conclusion is refuted in the West Virginia Supreme Court case *Virginia Electric and Power Company* v. *Haden*, —W. Va.—, 200 S.E.2d 848 (1973), U. S. cert. den. 416 U.S. 916, 94 S. Ct. 1624 (1974), and the United States Supreme Court case, *Utah Power and Light Co.* v. *Pfost*, 286 U.S. 165, 52 S. Ct. 548 (1932).

The facts and law in the West Virginia case are relevant to this analysis. Virginia Electric and Power Company (VEPCO) is a Virginia corporation, qualified to do business in West Virginia and North Carolina. It is a public utility providing electric power to the public primarily in Virginia and North Carolina and several small areas in West Virginia. The issues decided by the West Virginia Supreme Court were: (1) Is VEPCO a manufacturer of electricity subject to the West Virginia business and occupation tax, West Virginia Code section 11-13-2(b)? (2) Is the West Virginia business and occupation tax an undue burden on interstate commerce?

In deciding these issues, the West Virginia Supreme Court relied upon the *Utah Power and Light Co.* v. *Pfost*, *supra*, which held the manufacture of electricity, and its transmittal and sale are readily distinguishable. Manufacturing is a local activity, and not a part of interstate commerce. Commerce does not begin until the manufacture is finished.

In *Utah Power and Light Co.*, *supra*, the state imposed and sought to collect a license tax on the generation of electricity, even though such electricity was transmitted to an out-of-state consumer. It was contended that the imposition of such tax was unconstitutional as a burden on interstate commerce. The United States Supreme Court rejected this contention holding "(as) commerce does not begin until manufacture is finished, and hence the commerce clause of the (federal) constitution does not prevent the state from exercising exclusive control over the manufacture." See also *Crown Zellerbach Corporation* v. *State*, 45 Wash. 2d 749, 278 P.2d 305 (1954).

The West Virginia Court held, likewise, the manufacture of electricity is a separate and distinct local incidence occurring within the state. Therefore, VEPCO was subject to the West Virginia business and occupation tax (West Virginia Code section 11–13–2b) on its gross income derived from its intrastate manufacturing activity. The West Virginia court held the measure of the tax to be the gross receipts derived from the sale to the out-of-state buyer, less cost or receipts derived from the transmission or delivery thereof to the out-of-state consumer.

From this analysis, by both the Unites States Supreme Court and the West Virginia Supreme Court, it is apparent the Courts have made a clear distinction between electrical generation and its subsequent transmission outside the state. The West Virginia Court in *VEPCO*, *supra*, fully agreed electric power generated within West Virginia and sold without the state is a transaction in interstate commerce. But the West Virginia tax is on the manufacture of electrical power in West Virginia and the tax does not purport to tax the sale of electric power generated here and sold outside the state. This is the crucial distinction that must be made.

Generation and transmission of electrical power may be integral parts of the utility business, but clearly both are not integral parts of interstate commerce, according to the courts. Stated differently, a tax imposed on a local activity is valid if, and only if, the local activity is not such an integral part of the interstate process, the flow of commerce, so that it cannot realistically be separated from it. *Western Livestock* v. *Bureau of Revenue*, 303 U.S. 250, 58 S. Ct. 546 (1938).

ANALYSIS OF SECOND PREMISE OF S. 1957

The Supreme Court has long sustained unapportioned "doing business" taxes on total gross receipts from activtties carried on wholly within a state. The court treats these activities as taking place before the stream of interstate commerce. *American Mfg. Co.* v. *St. Louis*, 250 U.S. 459, 39 S. Ct. 522 (1919) (manufacturing); *Hope Natural Gas* v. *Hall*, 274 U.S. 284, 47 S. Ct. 639 (1927) (production of natural gas); *Oliver Iron Mining Co.* v. *Lord*, 272 U.S. 172, 43 S. Ct. 526 (1923) (mining). Therefofe, in continuing our analysis of Senate Bill 1957, its second premise is erroneous—that a privilege tax on generation of electricity is an unreasonable burden on interstate commerce.

Again, the West Virginia Supreme Court in *VEPCO*, *supra*, *and the United States Supreme Court in Utah Power and Light Co.*, *supra*, ruled that State is imposing a legitimate tax not in violation of the Commerce Clause, since generation is a distinct and separate incidence occurring within the tax jurisdiction, apart from the subsequent transmission in interstate commerce. There is no unreasonable burden on interstate commerce, because the subject of the tax is not interstate commerce, but rather a local incidence. And as previously shown, a local incidence cannot be an integral part of interstate commerce.

A long line of United States Supreme Court cases hold no undue burden is being placed on interstate commerce in such cases. In discussing the Commerce Clause, Article 1, Section 8, Clause 3 of the Federal Constitution, the United States Supreme Court has said: "It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though

it increases the cost of doing business." *Western Livestock* v. *Bureau of Revenue*, 303 U.S. 250, 254, 58 S. Ct. 546, 548 (1938).

"Even interstate business must pay its way," *Postal Telegraph-Cable Co.* v. *Richmond*, 249 U.S. 252, 259, 39 S. Ct. 265, 266 (1919).

A close study of the cases rendered by the United States Supreme Court on taxation of interstate commerce reveals the validity of a tax rests upon whether the state is exacting a constitutionally fair demand for that aspect of interstate commerce to which it bears a special relation. *General Motors Corporation* v. *Washington*, 377 U.S. 440, 84 S. Ct. 1564 (1964). In other words, the question is whether the state has exerted its power in proper proportion to the taxpayer's activity within the state and to the taxpayer's consequent enjoyment of the opportunitites and protection which the state has afforded. *General Motors Corporation* v. *Washington, supra.* As was said in *Wisconsin* v. *J. C. Penney*, 311 U.S. 435, 444, 61 S. Ct. 246, 250 (1940), "the simple and controlling question is whether the state has given anything for which it can ask in return."

It can be argued cogently that electric power companies located in West Virginia receive not only the ordinary and customary benefits of police and fire protection from government and the opportunity to seek redress in the judicial system, but they also benefit from the excellent natural resources in West Virginia—coal, gas, timber, stone, oil and waterways. These utilities consume the abundant natural resources of West Virginia. Should not they be asked to give something back in return to the State of West Virginia? The United States Supreme Court and the West Virginia Supreme Court have answered this question with a resounding—YES.

Senate Bill 1957 would prohibit a state from taxing electricity generated within it and transmitted without it, based upon the premises that (1) such activity is an integral part of interstate commerce and (2) such taxes impose an undue burden on interstate commerce. The courts have soundly rejected these two premises. As previously shown, the generation and transmission of electricity has traditionally been held by the courts to be a separate and distinct local incidence occurring within the state. Granted, that "it is beyond dispute that a state may not place a tax on the privilege of engaging in interstate commerce." *Northwestern States Portland Cement Company* v. *Minnesota*, 358 U.S. 450, 458, 79 S. Ct. 357, 362 (1959). But the Supreme Court has held that a taxpayer.s in-state activity may be a sufficient local incidence upon which a tax may be based. The Supreme Court held in *Spector Motor Service, Inc.*, v. *O'Connor*, 340 U.S. 602, 609, 71 S. Ct. 508, 512 (1951), "the state is not precluded from imposing taxes upon other activities or aspects of this (interstate) business which, unlike the privilege of doing interstate business, are subject to the sovereign power of the state."

Senate Bill 1957 will probably weaken some of the analytical tests used by the Supreme Court over the past forty years to determine the validity of state taxes. For example, if this legislation becomes law, the subject-measure, local incidence analytical tests espoused by the Supreme Court in dozens of cases over the years will be overturned regarding the manufacture and transmission of electricity. These tests would probably be weakened as applied to other manufacturing activities. Also, the multiple burden test, a leading analytical method, will be emasculated (*Western Livestock* v. *Bureau of Revenue, supra*).

In *Miller Bros. Company* v. *Maryland*, 347 U.S. 340, 344-345, 74 S. Ct. 535, 539 (1954), the Supreme Court stated the test succinctly by saying we must determine whether the tax is so closely related to the local activities of the corporation as to form "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." As previously shown by the case law, the generation of electrical power within a state is closely related to the state. There is a definite link, or connection, between the state and the subject of the tax. In West Virginia the subject is the privilege of manufacturing electricity in this state. Again, if the subject of the tax is a separate, distinct and local incidence apart from interstate commerce, then the initial measure of the tax may be the gross receipts derived from interstate commerce. *General Motors Corporation* v. *Washington, supra.*

In summary, S. 1957 is predicated upon a congressional finding that the generation of electricity, and its transmission to another state is an integral part of interstate commerce. Clearly, the courts have not agreed with this position.

Furthermore, S. 1957's second premise is erroneous—that a privilege tax upon the generation of electricity is an unreasonable burden on interstate commerce. Again, the courts have rejected this viewpoint, as long as the subject of the tax is a separate, distinct, local incidence occurring within the tax jurisdiction apart from interstate commerce. For instance, in West Virginia, the privilege tax is upon the manufacture of electricity in West Virginia. No other state can impose such a tax since the manufactur-

ing occurs in West Virginia. Thus, this tax passes all the tests used by the courts to uphold the validity of state taxes.

ANALYSIS OF THIRD PREMISE OF S. 1957

The third premise of the bill is erroneous—that a tax on electricity generated in one state and subsequently transmitted outside the state is a tax on the privilege of conducting interstate commerce. Again, the courts have rejected this viewpoint. Granted, a state cannot impose a tax on the privilege of conducting interstate commerce, but it can, according to the United States Supreme Court and the West Virginia Supreme Court, impose a tax on the privilege of conducting a business within the state, provided it is a separate and distinct local activity. Then, the gross receipts derived from the sale may be used to determine the value of the local incidence occurring within the tax jurisdiction.

EFFECT OF S. 1957 ON WEST VIRGINIA

Since the West Virginia Supreme Court and the United States Supreme Court have upheld the constitutionality of the West Virginia business and occupation tax on public utilities, and specifically on generators of electricity, this legislation would, in effect, overrule the longstanding decision of *Utah Power and Light Co.* v. *Pfost*, *supra*, and the recent *VEPCO*, *supra*. West Virginia has been, and is now, imposing a legitimate and constitutional tax. The *VEPCO* decision was denied certiorari to the United States Supreme Court in April, 1974 (416 U.S. 916). As previously shown, West Virginia is not attempting to tax an integral part of interstate commerce. Nor is it placing an undue burden on interstate commerce. And finally, West Virginia is not placing a tax on the privilege of engaging in interstate commerce. The *VEPCO* and *Utah Power and Light Co.* decisions clearly support this viewpoint.

DISTINGUISHING THE WEST VIRGINIA SITUATION FROM THE NEW MEXICO-ARIZONA SITUATION

The facts in New Mexico and Arizona are different than the facts in West Virginia. The West Virginia "business privilege tax" is measured by gross receipts and does not have credits like those disputed in the New Mexico-Arizona controversy.

In West Virginia, no similar credits are available to electricity producers for taxes imposed by other states, or for usage in West Virginia. As a matter of fact, in West Virginia, if an electricity producer transmits electricity outside the state, he is a manufacturer under our business and occupation tax law (West Virginia Code section 11-13-2b). There is a different business and occupation tax classification for strictly intrastate electricity producers, and they pay much higher taxes under the public utilities classification (West Virginia Code section 11-13-2d).

The measure of the lower tax on manufacturers is the value of the manufactured product here in West Virginia, and not the value of the product transmitted in interstate commerce.

Additionally, there is a benefit in the form of an industrial tax credit available to energy producers paying under the lower West Virginia Code section 11-13-2b manufacturing rate. It can eliminate up to 50 percent of the West Virginia business and occupation tax in any given year (West Virginia Code section 11-13C). Incidentally, Ohio Power Co. takes the full industrial tax credit in West Virginia thereby wiping out 50 percent of its business and occupation taxes on manufacturing.

Furthermore, this credit is not available to the energy producers within West Virginia paying their business and occupation tax under the substantially higher public utilities rate (West Virginia Code section 11-13-2d).

It should be noted that perhaps this amendment to Public Law 86-272 is an overreaction to deal with the specific situation existing between New Mexico and Arizona. By this attempt to eliminate the dispute between New Mexico and Arizona, many other states with "privilege or gross receipts taxes," or other similar taxes may be unintentionally prohibited from exacting their fair share of taxes commensurate with the government services provided, and the depletion of their natural resources and energy availability.

With this law, the Congress would preclude a state from taxing a separate and distinct privilege occurring within it that does not involve interstate commerce, according to the many Supreme Court cases previously cited. The law is clear that states can tax privileges being exercised within their jurisdiction, provided there is sufficient nexus to meet the due process of law requirements of the Fourteenth Amendment.

If this law is adopted, it will virtually destroy the manufacturing tax classification in West Virginia, not just for generators of electricity, but for other manufacturers. Our economy is so interrelated today that most goods travel in interstate commerce. And the Supreme Court has wisely espoused a test permitting states to tax local activity occurring intrastate prior to interstate commerce.

There is really no difference in the manufacture of electricity than the manufacture of any other commodity eventually entering interstate commerce. There is only a time element. Electricity generated may enter interstate commerce very soon after being manufactured, whereas a manufactured glass or an automobile may be in inventory for months before entering interstate commerce.

The analysis used by the Supreme Court in *Utah Light and Power Co.* v. *Pfost, supra*, explains the distinct aspects of generating and transmitting electricity, and why the two activities are separate.

First, there is a conversion of energy into electrical energy, and, second, there is transmission. Conversion and transmission are substantially instantaneous, but they are separate activities and not simultaneous activities. There is a conversion of energy into electrical energy, and this conversion must occur before the energy can be transmitted. The transformation is complete at the generator in the state of origin.

The manufacture of goods and their immediate shipment to the purchaser is a helpful analogy. The goods must be manufactured before they can be sent. The manufacture of electricity is essentially no different than the manufacture of any other product, except that electricity is not a tangible substance having length, width, or thickness and purchased in yards or gallons.

In effect, this law would restructure the entire West Virginia tax system. It would result in discrimination against all other manufacturers by giving the manufacturers of electricity a special tax exempt status. It may force West Virginia to go to higher corporate net income taxes, or raise other taxes to compensate for the lost revenue.

In West Virginia, the business and occupation tax is our largest revenue producer. Such a law, as now contemplated by Congress, would obviously result in lower state revenues. In a tine when the public is demanding more and better services from government, the only alternatives are: (1) increase taxes, or (2) cut back these government services. Build fewer highways, hospitals, and schools, and spend less for education. If the choice is to keep government services where they are, or increase them, the revenue loss must be made up by increasing our personal income tax, the consumers sales tax, the property tax, or the excise taxes of West Virginia. Possibly, there would be a return to more regressive taxes like the property and consumers sales taxes.

With West Virginia's abundant natural resources being used in the production of electricity, it seems unfair that the state cannot ask for something in return for the consumption of those finite, valuable resources.

Is it fair to ask West Virginians to subsidize the production of electricity used in other states, resulting in lower rates for them, but higher taxes upon ourselves?

Is it fair to ask West Virginians to expend valuable resources for someone else's benefit without receiving some just measure of return?

It is important to note that over 70 percent of the electricity manufactured in West Virginia is transmitted to other states. Consequently, our resources would continue to be depleted without a fair return on those resources. Remember that Justice Clark in *General Motors Corporation* v. *Washington, supra*, stated the question is whether the state has given anything for which it can ask in return.

POSSIBLE EFFECT OF S. 1957 ON OUR FEDERAL FORM OF GOVERNMENT

Another important consideration may be the effect of this law on our federal system of government. Would not Congress be placed in the position of taking away the states' power to tax a privilege occurring within their own borders? By depriving West Virgiria and other states of their right to tax a local privilege occurring within their jurisdictions, Congress would remove a substantial portion of the states' taxing power. By removing the states' power to tax, the Federal Government may remove the states' means to create, not only strong state governments, but viable programs to deal with the problems facing America in its third century.

Consequently, the Federal Government may totally become the financial well for the states unable to cope properly with their revenue problems as a result of this legislation.

Senator FANNIN. The record will be open for further comments. The record will be open for 4 weeks as usual.

This concludes the hearings at this time.

We thank you for coming.

[Whereupon, at 3:30 p.m., the subcommittee adjourned, subject to the call of the Chair.]

[By direction of the chairman, the following communications were made a part of the printed record:]

STATEMENT BY MARY ELLEN MCCAFFREE, DIRECTOR, WASHINGTON STATE DEPARTMENT OF REVENUE

TAXING THE GENERATION OF ELECTRICAL ENERGY

The following statement represents the position of the State of Washington on Senate Bill 1957, which would prohibit states from taxing the generation of electrical energy to the extent that such energy is exported outside their boundaries. Senate Bill 1957 received a hearing before the Senate Finance Subcommittee on Energy March 8, and it is requested that this statement be included in the record of that hearing.

The State of Washington is opposed to Senate Bill 1957 for the following reasons:

1. It would result in an immediate adverse revenue impact for the state, and an increasing debit as the state expands its energy generating industry.
2. It would create an inequity among taxpayers similarly situated (i.e., companies generating power for instate consumption would be subject to state taxation and those companies generating power for export would have no state tax liability).
3. It would set a precedent for exempting other businesses which manufacture commodities for eventual entry into interstate commerce (at a significant revenue loss to the state) for government services, replenishing of natural resources and compensation for destruction of the natural environment.

What the bill means for Washington

The restrictive impact of Senate Bill 1957 on Washington tax laws is achieved by denying states the right to distinguish between the generation of electrical energy and the transmission of energy to out of state consumers. Briefly, the bill states:

1. The generation and transmission of electricity from one state to another are integral parts of interstate commerce.
2. Any privilege tax on the generation and transmission of electricity from one state to another is an unreasonable burden on interstate commerce.
3. No state has the power to tax the privilege of conducting interstate commerce activity if the tax is on the generation of electricity within a state which is then transmitted without the state.

For the purpose of determining state tax liability, Washington treats the generation of electrical energy destined for export like any other instate manufacturing of commodities which

4. It would terminate any method the state may undertake to ensure that the industry provides some compensation for the costs of development of this industry, in terms of required state and local services, depletion of natural resources and impact on the environment.

The State of Washington is a substantial producer and net exporter of electrical energy. It ranks 6th among all states in production of electrical energy and generated 4.85 percent of the nation's total electrical energy output in 1974. Approximately 22 percent of all electrical energy generated in Washington is exported. (This includes energy generated by the Bonneville Power Administration at Grand Coulee and other sites, even though the state does not presently levy a tax on the substantial portion of the Bonneville output that is exported across state lines.) The proposed siting of seven new nuclear energy facilities in the state (three at Hanford, two at Satsop and two in Skagit County) will continue to expand the role of Washington State as a major provider of energy for the nation.

Senate Bill 1957 would deny citizens of this state realization of benefits commensurate with the state's investment for development of the energy producing industry and would cut off any opportunity the state might have for recovering the costs to the residents of this state, in terms of reimbursement evenutally enter interstate commerce. Businesses producing electrical power for export pay the same tax that other manufacturers of export goods pay. The only basis for treating the generation of electrical energy differently than the manufacture of other export products would be the element of time between the production (or manufacturing) activity and eventual delivery outside state borders. In the case of energy, the conversion and transmission processes are substantially instantaneous, occurring at the generator, whereas with other commodities the production and delivery occur in a much longer time frame. By denying the states the right to distinguish between production and transmission of energy, Senate Bill 1957 would place energy in a special category, separate and apart from other products entering interstate commerce. This runs counter to the interests of the states which serve as energy resources for the nation and would overturn several important court decisions which have supported the rights of states, under the federal Commerce Clause, to levy a state tax on the business of generating electricity where the electricity is sold out of state. (Notably, *Utah Power & Light Co.* v. *Pfost*, and *Public Utility District No. 2 of Grant County, et al* v. *Washington*. The West Virginia

Supreme Court also recently upheld that state's privilege tax on the business of generating electricity in the case of *VEPCO* v. *Haden*.)

WASHINGTON'S TAX STRUCTURE

The State of Washington has no income tax and depends entirely on the sales and excise taxes and various business privilege taxes for revenue. Companies generating electrical energy for export are subject to the state business and occupation tax. This is not a tax on interstate commerce, but rather a privilege tax levied on all industry doing business in the State of Washington (including manufacturers of other commodities destined for export). The rate is low (.44 percent) and does not represent a "unreasonable burden" on interstate commerce. By comparison, power companies generating electricity wholly for instate consumption pay the much higher utilities tax which carries a rate more than eight times (3.6 percent) greater than the business and occupation tax.

In treating the generation of electrical energy for export like any other instate manufacturing activity, Washington tax law provides an incentive for the export of electrical energy, while at the same time recognizing the need to maintain a meaningful revenue source to compensate the citizens of the state for services and resources consumed by the industry. This treatment has received the consent of Washington power companies, which used the manufacturing analogy as part of their arguments before the Washington Legislature for preferential tax treatment. Partly in recognition that the exporting power companies may be subject to the tax laws of receiving states, the Legislature agreed to the analogy and granted the much lower business and occupation tax rate.

Revenue Loss

Provisions of Senate Bill 1957 would allow state tax laws to apply only to that portion of electrical energy wholly consumed within the state. Although the state tax rate on exported energy is low and not a great revenue producer at this time, deletion of this revenue source would bar the state from requiring one segment of the industry to contribute some compensation for costs to the state incurred in past and future development of the industry. In fiscal year 1975 the state received approximately $315,000 from the tax imposed on the business of electrical energy sold out-of-state. The loss of this revenue source, as provided in Senate Bill 1957, would require a proportionate shift of the tax burden to other Washington taxpayers. More importantly, exemption of such energy generation activity from state tax liability reduces the incentive for states, such as Washington, to develop energy resources to meet the needs of other states. Further, it sets an adverse precedent for state taxation of other manufacturers of export commodities, which does represent a sizable portion of Washington's current tax base. (Approximately 20 percent of the state's major business tax revenue is paid by manufacturers of exported goods, and amounts to $102 million for the 1975–77 biennium.) It should also be noted that the seven nuclear energy generating facilities now planned for Washington would fall within provisions of Senate Bill 1957, which would considerably increase the revenue impact beyond what it would be immediately.

The exemption from state tax for the generation of exported energy could encourage increased exportation against the best interests of Washington residents. If Senate Bill 1957 were enacted at this time it would be cheaper to manufacture electricity for sale outside the state than for sale to Washington residents. The net result could be less energy available to Washington citizens, and additionally at a higher cost. Thus, Washington consumers would carry the burden of a revenue loss and would also be subject to higher rates for electrical energy than their neighbors in adjoining recipient states.

The Question of Equity

Senate Bill 1957 would place the State of Washington in a position of discriminating unfairly against businesses similarly situated, through what amounts to selective application of state tax laws. To provide an exemption from state tax laws on the basis of final destination of the product gives one business an unfair competitive advantage over another engaged in a similar activity—the generation of electrical energy. All electrical energy generating companies in Washington are engaged in the same activity and use the same state resources and services. Yet, under provisions of Senate Bill 1957, only those companies selling to the local market would be required to contribute to the support of government services and the replenishing of the state's natural resources.

Consumption of State Resources

The tax exemption provided by Senate Bill 1957 would permit consumption of the state's natural resources and impose environmental costs without due compensation. Hydroelectric generation, although relatively pollution free, destroys or severely limits the fishery resources of the anadromous variety (e.g., Salmon, Steelhead) for sport and commercial fishing. In addition to the decimation of an immensely valuable fishery resource, the presence of large hydroelectric generating facilities represents an additional cost to the citizens of the state in terms of defacing the natural environment. Fossil fuel generation, typically coal, results in scarring of the landscape from strip mining, destruction of wildlife natural habitat and increased air pollution. Nuclear energy generation, although it does not consume natural resources, results in thermal pollution of rivers and lakes and exposes people to the possible risk of accidents, radiation leaks and catastrophic destruction in the area surrounding the generation facility.

Conclusions

The State of Washington recognizes that for many purposes natural resources which are consumed in the generation of electrical energy are properly regarded as national resources, rather than the sole property of any particular state. However, it is clear that the environmental costs and burdens attendent upon consumption of these natural resources are visited primarily upon the people of the state in which the resources are located. Provisions of Senate Bill would require Washington residents to bear the environmental and economic costs and subsidize the benefits to people of other states without any compensation.

Washington state taxes on the generation of electrical energy consumed outside the state are not confiscatory, nor do they increase significantly the costs of that energy to consumers in recipient states. The Washington business and occupation tax can not represent an adverse economic impact on national commerce so as to justify federal interference with the ability of the host energy resource states to realize some benefits from their investment in the industry. We urge defeat of Senate Bill 1957.

PAINE, LOWE, COFFIN, HERMAN & O'KELLY,
Spokane, Wash., April 2, 1976.

Re: S. 1957

MR. MICHAEL STERN,
Committee Staff Director,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: We are counsel for The Washington Water Power Company of Spokane, Washington, a utility company primarily engaged in the production, transmission and distribution of electricity in eastern Washington, northern Idaho and western Montana and in the distribution of natural gas in eastern Washington and northern Idaho. As such counsel, we were involved in litigation challenging taxes imposed by the State of Washington on electric energy sold for export and are presently involved in litigation in Montana and Idaho involving similar taxes.

It is understandable that states hard pressed for money will be tempted to raise money painlessly by imposing taxes paid solely by taxpayers of another state. It is also the function of the United States through constitutional or legislative processes to prevent the states from placing artificial economic barriers at state lines.

We, therefore, support the general intent of S. 1957. However, it appears to go too far as presently drafted. The title to Title II refers to "Discriminatory Taxes" but the substantive provisions appear to prohibit all taxes.

The New Mexico tax is one that appears to us to be patently discriminatory. We understand that New Mexico justifies its tax, in part, by reference to the Washington tax. The practical operation of the Washington and New Mexico statutes is quite different. In Washington there is a 3.6 percent tax at the retail level. The retail price includes manufacturing costs and transmission costs as well as distribution costs. Sales at wholesale involve only the manufacturing costs and transmission costs to the point of delivery which then incur a 3.6 percent tax on those functions only when the power is exported. In *Pud No. 2 of Grant County* v. *State*, 510 P.2d 206, the Washington Supreme Court upheld a tax on the sale at wholesale of electricity to be exported from the State. However, the 3.6 pecent tax was applied to export power that sold in the neighborhood of 5 mills while it was selling at retail at anywhere from two to three times that much and the same rate of tax is applied to retail sales. Applying 3.6 percent to 5 mills results in a tax of $.00018 per kwh. Applying

3.6 percent to 1.5 cents results in a tax of $.00054 or three times the tax applied to export power. Even this was considered unfair by the Washington Legislature because it resulted in a manufacturing tax much higher than other manufacturing taxes. In 1965, while the court case was pending, the rate applied to manufacture of electricity which is paid only on export power was reduced by the Legislature to .44 percent. Applying this to 5 mills results in a tax of $.000022 per kwh, which makes the New Mexico tax over 18 times the tax now charged by Washington.

In summary, the principal point of difference is that Washington bases its tax on the value of the product at each stage and picks up the value on a proportionate basis at the manufacturing state in its tax on retail sales in the state. As the Washington Court, in *PUD No. 2 of Grant County* v. *State* pointed out, ". . . the tax deduction that is made at the sale to a Washington utility is made up at the time the Washington utility buyer sells to its customers." The .4 mills per kwh levied by New Mexico, being completely arbitrary and with a direct credit to local utilities up to and including their entire liability under the Gross Receipts Tax, *in its practical operation* does "work a discrimination against interstate commerce." It lacks the automatic apportionment of the Washington statute and the tax is not apportioned to the business done in the state.

Since the United States is moving into a period of energy shortage and since the supply of energy is not evenly distributed, the Congress should address two aspects of the problem.

First is the prevention of discrimination against interstate commerce which may be prevented in the courts by enforcing the Constitution.

Second is the prevention of discrimination against energy sources. A state should be able to levy a manufacturing tax on electricity or other forms of energy but the amount of the tax should be reasonably related to the burden imposed on the state by the manufacturing or other process. The tax rate should be comparable to the rate of taxes levied on other comparable business as it is presently in the state of Washington.

The Congress should also consider expanding the studies proposed to include other forms of energy. Confiscatory taxes placed on coal, oil, natural gas, uranium, etc. will compound the nation's energy problems. It is particularly in the area of discrimination against energy as contrasted with discrimination against interstate conmerce that the courts will not be able effectively to provide solutions and the Congress will be the only body having the authority to do so.

Thank you for this opportunity to express our views.

Very truly yours,

PAINE, LOWE, COFFIN, HERMAN & O'KELLY,
By Alan P. O'Kelly.

SOUTHERN CALIFORNIA EDISON COMPANY,
Washington, D.C., March 3, 1976.

Hon. MIKE GRAVEL,
Chairman, Energy Subcommittee,
Committee on Finance,
Dirksen Senate Office Building,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: S. 1957 by Mr. Fannin would prohibit any state from imposing a tax on the generation of electricity to the extent that such electricity is transmitted to and consumed outside of such state. This bill would have a direct and substantial economic impact on Southern California Edison Company and its consumers. We urge the passage of S. 1957.

By way of background, Edison is a public utility primarily engaged in the business of supplying electric energy in portions of central and southern California. Its service area covers about 50,000 square miles with an estimated population of 8,000,000. In addition to hydroelectric, nuclear and fossil fueled generating plants located in California, Edison also has major generating resources in other states. These include a 48 percent interest in the Four Corners Project in New Mexico, and a 56 percent interest in the Mohave Project in Nevada. Edison is a participant in the proposed Kaiparowits Coal Project in Utah and the Palo Verde Nuclear Project in Arizona. The Company also makes major purchases of energy from out-of-state sources, principally the Pacific-Northwest and the Navajo Project in Arizona. In 1975, almost 25 percent of the energy sold by Edison to customers in California came from outside the state.

As you are aware, the State of New Mexico passed a law imposing a tax on the generation of electricity starting July 1, 1975. That law allows a credit for the generation tax against the state tax on sales of electricity to consumers in New Mexico. The practical effect is to exempt all electric customers within New Mexico from the tax on generation and impose it only on the electric utilities serving customers outside of New Mexico. The amount of this tax imposed on customers of Southern California Edison Company in California is approximately $1,600,000 per year.

The electric utilities serving customers affected by this tax feel that this legislation is unconstitutional because it discriminates against electricity being transmitted in interstate commerce. They have instituted legal action to seek nullification of the New Mexico tax in order to protect their customers against higher electric rates and the unfair treatment which results from the New Mexico tax. In addition, the State of Arizona has brought suit against the State of New Mexico in the United States Supreme Court to invalidate the New Mexico tax.

The most efficient use of this nation's energy resources requires that the coordination of generating resources in the several states be optimized. Taxes such as those imposed by New Mexico which hamper and impede the selection and use of the most efficient and economic resources available to serve the public will tend to defeat this objective and is contrary to the public interest.

For these reason's we support the passage of S.1957. We wish to thank you for the opportunity to express our views and respectfully request that they be included in the Hearing Record.

Very truly yours,

ALAN M. NEDRY.

STATEMENT BY RICHARD S. WEYGANDT, VICE PRESIDENT, MONONGAHELA POWER COMPANY

The following statement is presented on behalf of Monongahela Power Company, West Penn Power Company and The Potomac Edison Company, operating companies of the Allegheny Power System. Monongahela serves customers in West Virginia and Ohio, Potomac Edison serves customers in West Virginia, Pennsylvania, Maryland and Virginia and West Penn serves customers in Pennsylvania. All three companies have ownership in power stations in West Virginia.

We did not have advance awareness of the hearing on S. 1957 which was had two weeks ago before the Energy Subcommittee, so I am taking the liberty of now submitting these comments in the hope of providing some background information which may be helpful to your committee in assessing the bill's impact. The Allegheny Power System companies would like very much to see S. 1957 enacted for the following reasons.

The bill is one which proposes to prohibit a state from taxing electricity which is generated within that State and transmitted to another state for consumption there. As you doubtless know, the subject attracted attention when New Mexico last year imposed a tax on electricity generated in New Mexico and sold in Arizona. At the present time some people in West Virginia are evincing interest in similarly increasing the state business and occupation tax on electricity generated in West Virginia and sold out of state. There is presently pending in the state legislature a bill (S. B. 572) which would raise such tax from its present rate of .88 percent of the gross proceeds derived from such sales to 3 percent of such proceeds.

We maintain that an increase in the tax on West Virginia-generated electricity which is sold out of state will actually hurt customers of Monongahela and Potomac Edison in West Virginia as well as customers of West Penn in Pennsylvania and customers of Potomac Edison in Pennsylvania, Maryland and Virginia, and it is to the advantage of all those customers to hve such tax kept at a minimum or eliminated completely. In addition, to the extent that such tax discourages out-of-state electric utilities from continuing to build power stations in West Virginia to serve their out-of-state customers, the future of West Virginia's coal industry will be threatened as well as the state's future industrial development.

Let me refer first to the example of an electric utility generating in West Virginia, such as Monongahela, which serves West Virginia customers and which occasionally also sells to out-of-state utilities. When Monongahela builds a new power station in West Virginia it does so because the increased generating capacity is needed to enable it to meet the increasing peak demands of its customers. During times when customer demand is below peak, a portion of the Company's available capacity is not being used (particularly immediately following completion of a new power station). In order

to avoid saddling its own West Virginia customers with the full cost of maintaining such idle capacity, the Company endeavors to sell it to other utilities at a profit.

An out-of-state utility will purchase such so-called economy power from Monongahela only when Monongahela's cost of generating the power is less than the out-of-state utility's own cost of generation. When a sale is made, the difference between the two costs is divided equally between the participating companies so that both benefit. The profit realized by Monongahela from such a sale is then credited against the expense of serving West Virginia customers, thus in effect keeping their rates to a minimum. Without such out-of-state sales, West Virginia customers would have a greater generating capacity cost to bear.

Such transactions also occur in reverse, when Monongahela buys unused capacity from out-of-state utilities needed to meet a temporary surge in the demands of its West Virginia customers. By increasing the tax on electricity generated within the state for out-of-state sales West Virginia will add to the cost of such electricity which must be borne by customers of the purchasing utility through higher rates. The states in which the purchasing utilities are located can be expected to retaliate by increasing the tax on electricity generated in those states and sold to Monongahela in West Virginia—thus necessitating higher rates in West Virginia.

Let me refer now to the example of an out-of-state electric utility, such as West Penn, generating in West Virginia whose customers are located outside West Virginia. (78 percent of Potomac Edison's customers are also located outside of West Virginia.) Obviously the rates of those customers will have to be increased to absorb the West Virginia tax on the electricity generated in West Virginia for their consumption. However, there is a further effect which can be predicted which will multiply the injury to the state's economy and future industrial development.

West Virginia is, as you know, a major source of coal for the entire country. Because of its plentiful supply of coal, electric utilities serving customers in other states—such as Appalachian Power, Ohio Power and Vepco in addition to West Penn and Potomac Edison—have constructed power stations in West Virginia to be near such supply and to avoid high fuel transportation costs. As a consequence, West Virginia's coal industry has benefited measurably and industry has been attracted to West Virginia by its lower electric rates.

Within the past 10 years, the Allegheny Power System companies have constructed two major power stations (Fort Martin and Harrison) in West Virginia and a third (Pleasants) is currently under construction. The annual coal consumption of each of these stations is approximately 3 million tons per year. Each of these stations, upon completion, thus provides employment for approximately 800 coal miners whose annual wages total more than $10 million. If West Virginia, through its taxing power, increases the cost of West Virginia-generated power to customers of the out-of-state utilities named above, those utilities in the future are certainly going to look for sites near coal reserves in states other than West Virginia on which to construct further new power stations. West Virginians would then begin to find themselves having to rely more and more on imported power at resulting higher rates made necessary by required additional transmission facilities.

Power station construction itself provides a significant benefit to West Virginia. The Pleasants station will cost $681 million and will employ as many as 1,800 construction workers with an average annual payroll of $37,500,000 over a period of 4 years. Upon completion, the station will employ 130 operating employees with an annual payroll of nearly $2 million.

We believe, therefore, that if West Virginia and other states are allowed to tax sales of locally-produced electricity sold in other states, all electric utility customers will eventually find themselves paying higher electric rates because, with respect to local electric utilities serving local customers, the resulting high price of electricity which those utilities will have to charge out-of-state utilities will discourage purchases by such utilities; without the revenues from out-of-state sales to help carry the cost of unused generating capacity between periods of peak demand, local (intrastate) rates will have to be increased to reflect such cost. We believe also that the future of the coal industry and industrial development generally in West Virginia and similar coal-supplying states would suffer greatly if a tax-induced increase in the price of electricity generated within a state by out-of-state utilities for sale to their out-of-state customers would discourage further power station construction in such coal-rich states.

I hope that you will give serious consideration to the above factors in evaluating S. 1957 and that you will conclude that its passage would not only forestall retaliatory taxation by the various states but would in fact serve as an anti-inflationary curb on utility costs to the benefit of ratepayers in all the states.

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