STATE OF NEW MEXICO
ADMINISTRATIVE HEARINGS OFFICE
TAX ADMINISTRATION ACT

IN THE MATTER OF THE PROTEST OF
APACHE CORPORATION & SUBSIDIARIES
TO ASSESSMENT ISSUED UNDER
LETTER ID NO. L1272612144

v. **AHO D&O No. 21-21**

NEW MEXICO TAXATION AND REVENUE DEPARTMENT

DECISION AND ORDER

On May 6, 2019, May 7, 2019, May 8, 2019, and May 9, 2019, Chief Hearing Officer Brian VanDenzen, Esq. of the Administrative Hearings Office conducted a merits administrative hearing in the matter of the tax protest of Apache Corporation & Subsidiaries (Taxpayer) pursuant to the Tax Administration Act and the Administrative Hearings Office Act. At the hearing, attorneys Anthony TJ Trujillo, Frank Crociata, Gene Creely, and Kelly Mooney appeared and represented Taxpayer. Attorney David Mittle appeared and represented the opposing party in the protest, the Taxation and Revenue Department (Department).

This protest involves multiple complex aspects of state corporate income taxation of a multinational oil and gas production company: whether Taxpayer's foreign subsidiaries are unitary corporations with Taxpayer; whether certain sources of income are considered business or non-business income for purposes of New Mexico apportionment; whether an apportioned share of a combined group of unitary corporations' foreign dividend income, Subpart F income, and other deemed foreign subsidiary income, is subject to New Mexico corporate income tax; whether New Mexico's treatment of foreign subsidiary income violates the Foreign Commerce Clause or the Equal Protection Clause of the Constitution; and, if liable for the assessed corporate income tax, whether Taxpayer made a mistake of law, entitling Taxpayer to abatement of the assessed penalty.

Ultimately, while Taxpayer is entitled to the Department's proposed 30% exclusion alternative apportionment method to address the obvious distortion under the original assessment, removal of the non-unitary dividends generated by one subsidiary, and abatement of civil negligence penalty, Taxpayer's protest is otherwise unpersuasive.

Taxpayer called John W. Sauer, C.P.A., as a witness. The Department called Corporate Income Tax Auditor Dan Armer, C.P.A., and Protest Auditor Mary Griego as witnesses in this matter. Taxpayer Exhibits #1-7, #11-20, #23-25 were admitted into the record. Taxpayer exhibits #8-10, #21 (withdrawn), and #22 were not admitted into the record. Department Exhibits B-L, N-Q, S, T, V-Z, AA, AC-AF, AH, and AJ were admitted into the record. Department Exhibits A, M (no exhibit tendered), R (no exhibit tendered), U (no exhibit tendered), AB (withdrawn, same as Taxpayer Exhibit #24), AG, and AI were not admitted into the record. All exhibits are more thoroughly described in the exhibit log contained in the record.

IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

Jurisdictional Background

1. On March 31, 2017, the Department issued Taxpayer a notice of assessment of corporate income tax for the 2015 reporting period. Under that notice of assessment, Taxpayer owed $24,187,441.00 in corporate income tax, $2,418,744.10 in civil penalty, and $963,494.45 in interest for a total assessed liability of $27,569,679.55. [Taxpayer Ex. #7; Administrative Record, hearing request packet; 5/6/19 Tr. 206:12-23].

2. On June 28, 2017, Taxpayer protested the assessment. [Taxpayer Ex. #11; Administrative Record, hearing request packet].

3. On July 18, 2017, the Department acknowledged receipt of Taxpayer's protest. [Administrative Record, hearing request packet].

4. On August 29, 2017, the Department requested a hearing with the Administrative Hearings Office on Taxpayer's protest. [Administrative Record, hearing request packet].

5. On September 8, 2017, a scheduling hearing in this matter occurred within 90-days of the hearing request. At that hearing, neither party objected that conducting the hearing satisfied the 90-day statutory hearing requirement. [Administrative Record].

6. On April 2, 2018, Taxpayer filed an amended 2015 CIT-1 return. [Taxpayer Ex. #8].

7. On June 5, 2018, Taxpayer filed an amended protest of the assessment. The amended protest made no mention of a Taxpayer's filing of an amended 2015 CIT-1 return. [Taxpayer Ex. #12].

8. The evidentiary merits hearing in this matter occurred on May 6th through 9th, 2019. In addition to the Administrative Hearings Office digital recording of that proceeding, Taxpayer had the entire proceeding transcribed. A copy of each day's transcription is part of the administrative record. All citations to testimony are to the transcripts provided by Taxpayer. [Administrative Record].

9. The Department objected during the hearing that Taxpayer's amended 2015 CIT-1 return was outside the scope of the protest. [5/6/19 Tr. 27:19-23].

10. Both Taxpayer's original protest or amended protest focused on the original assessment issued related to Taxpayer's original 2015 CIT-1 return. Neither Taxpayer's original protest nor amended protest mentioned, addressed, or discussed Taxpayer's amended 2015 CIT-1 return. [Administrative Record, hearing request packet].

11. Because the protest letter and amended protest letter did not raise Taxpayer's amended 2015 CIT-1 returns as grounds of the protest, the hearing officer ruled as a preliminary matter that only the original 2015 CIT-1 return was at issue in this protest. [5/6/19 Tr. 59:18-61:6].

12. Taxpayer agreed to adjust its hearings exhibits to address the numbers contained in its original 2015 CIT-1 return and the Department agreed that it would apply the legal determinations made in this protest related to the original 2015 CIT-1 return to Taxpayer's amended 2015 CIT-1 return. [5/6/19 Tr. 27:19-23; 41:18-61:6].

13. The parties filed their written closing arguments on November 15, 2019, completing the hearing on that date and making the matter ripe for a decision[1]. In addition to its written closing argument, Taxpayer provided proposed findings of fact and conclusions of law. [Administrative Record].

Witness Background

14. John Sauer, C.P.A., is Senior Vice President of Tax for Taxpayer. He has a bachelor's degree in accounting from the University of North Dakota. Mr. Sauer has 37-years of experience in the oil and gas tax field and has been employed by Taxpayer for 26 years. Mr. Sauer is responsible for Taxpayer's federal and state tax compliance, as well as tax accounting for the company's federal Securities and Exchange Commission (S.E.C.) filings. [5/6/19 Tr. 197:17-198:15].

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[1] Under *Kmart Props., Inc. v. Taxation & Revenue Dep't*, 2006-NMCA-026, ¶55, 139 N.M. 177, 192, *rev'd on other grounds and certiorari as to corporate income tax issues quashed, Kmart Corp. v. Taxation & Revenue Dep't.*, 2006-NMSC-006, 139 N.M. 172., delay in issuing a decision beyond 30-days does not invalidate the authority or jurisdiction of hearing officer to decide a complex, high-magnitude tax protest case. Like *Kmart Props*, this case was a high-magnitude, complex corporate income tax protest involving multiple issues, thousands of pages of exhibits, a four-day hearing, and an extensive post-hearing six-month briefing period. *See also Ranchers-Tufco Limestone v. Revenue*, 1983-NMCA-126, ¶13 (delay in action is not a defense to enforcement in a tax action).

15. Mr. Sauer serves as a corporate officer for Taxpayer as well as all of Taxpayer's relevant subsidiaries. He also sits on the board of directors of most of Taxpayer's subsidiaries, including Taxpayer's relevant foreign subsidiaries. [5/6/19 Tr. 202:12-19].

16. As of the date of hearing, Dan Armer, C.P.A., was a tax auditor with the corporate audit department of the Taxation and Revenue Department. He had been employed at the Department for 21 years, 19 of which were with the corporate audit unit. Mr. Armer represents the Department on various Multistate Tax Commission committees. [5/8/19 Tr. 39:4-40:8].

17. Mary Griego is a protest auditor with the Taxation and Revenue Department. She has held that position for approximately six years. She was assigned Taxpayer's protest for review around June of 2017. [5/8/19 Tr. 179:17-180:13].

General Nature of Taxpayer's Business Operations

18. Taxpayer is a publicly traded, multinational corporation engaged in the business of petroleum and natural gas exploration and production. Taxpayer is based in Houston, Texas. Taxpayer performs oil and gas exploration and production in the United States and across the globe, including in Argentina, Australia, Canada, Egypt, and the United Kingdom. [Taxpayer Ex. #18; 5/7/19 Tr. 36:14-37:14; 43:1-20].

19. Taxpayer has approximately 3,500 employees, with between 2,000-2,500 stationed in Houston, Texas and the remaining 1,000-1,500 employees stationed outside of Houston. [5/7/19 Tr. 262:10-262:18].

20. Taxpayer began operations in the United States upon its founding in 1954, in Australia in 1991, in Egypt in 1994, in Canada in 1995, in the United Kingdom in 2003, and in Argentina in 2008. [5/7/19 Tr. 37:5-14].

21. In each of these global regions or countries, Taxpayer typically conducts its operations through a combination of holding companies, financing companies, and operating companies, though not every country has its own financing entity. [5/7/19 Tr. 37:15-38:3].

22. Taxpayer conducts its petroleum and natural gas exploration and production activities through a number of domestic (U.S.) and foreign (non-U.S.) subsidiaries. [Taxpayer Ex. #18.2].

23. Relevant to the issues in this protest are 15 of Taxpayer's foreign subsidiaries that paid a foreign dividend, generated Subpart F income, or otherwise generated check-the-box income in 2015. Those 15 entities, along with a brief summary description of their roles, are:

a. Apache Energy Limited, an Australian oil and gas exploration and production company with numerous operating subsidiaries of its own [5/7/19 Tr. 62:13-63:5];

b. Apache Lowendal Pty Limited, another Australian oil and gas exploration company but without any subsidiaries [5/7/19 Tr. 63:6-15];

c. Apache UK Limited, a holding company [5/7/19 Tr. 63:16-24];

d. Apache Australia Management General Partnership, a financing entity that financed Australian oil and gas exploration and production. This entity also had other subsidiaries [5/7/19 Tr. 64:1-12];

e. Apache Australia Management Finance General Partnership, another financing entity that financed Australian oil and gas exploration and production. This entity also had other subsidiaries [5/7/19 Tr. 64:13-23];

f. Apache Canada Funding I Limited Partnership, a financing entity that financed Egyptian oil and gas exploration and production [5/7/19 Tr. 64:24-65-13];

g. Apache Canada Funding III Limited Partnership, another financing entity that financed Egyptian oil and gas exploration and production [5/7/19 Tr. 65:14-21];

h. Apache Egypt Investment Corporation LDC, serving as a general partner in a partnership with Sinopec in Egypt [5/7/19 Tr. 65:22-66:11];

i. Apache Finance Egypt I S.a.r.l., a holding company for oil and gas operations in Egypt and Canada [5/7/19 Tr. 66:12-18, 69:20-70:16];

j. Apache Egypt Holdings III Corporation LDC, a holding company for oil and gas operations in Egypt [5/7/19 Tr. 67:1-13];

k. Apache Egypt Holdings IV Corporation LDC, another a holding company for oil and gas operations in Egypt [5/7/19 Tr. 67:14-19];

l. Apache Asyout Corporation LDC, an Egyptian oil and gas company [5/7/19 Tr. 68:5-13];

m. Apache International Holdings S.a.r.l., a holding company for entities in Argentina, Australia, and the United Kingdom [5/7/19 Tr. 68:14-20];

n. Apache UK Corporation LDC, a holding company for United Kingdom oil and gas operations [5/7/19 Tr. 68:21-69:1]; and

o. Oil Insurance Limited, an insurance co-op for Gulf of Mexico oil and gas companies in which Taxpayer has less than a 5% stake. [5/7/19 Tr. 69:2-22];

[Taxpayer Ex. #15.3; 5/7/19 Tr. 56:19-70:19].

24. Of those 15 entities described in the previous finding of fact, Taxpayer wholly owned all but one, Oil Insurance Limited. [Taxpayer Ex. #15.3; Taxpayer Ex. #4; 5/7/19 Tr. 88:4-10].

25. None of the 15 entities that generated foreign dividends or Subpart F income operated in the United States during 2015. [Taxpayer Ex. #2.4; 5/7/19 Tr. 89:22-91:21].

26. The foreign dividends at issue in this case generally started accumulating in 1991, the year when Taxpayer acquired the first relevant foreign subsidiary, Apache Energy Limited, through tax year 2015.

Unitariness of Taxpayer's Foreign Subsidiaries

a. *General Evidence of Unitariness*[2]

27. The Department's February 13, 2017, "Request for Additional Information," sent to the same address listed by Taxpayer on its CIT-1 return, asked that Taxpayer complete the "Foreign Dividend and Subpart F Income Payor Business Connection Questionnaire" by March 18, 2017. The answers to that questionnaire can potentially assist in determining whether a unitary relationship exists between corporate entities. [Dept. Ex. AH; 5/6/19 Tr. 223:9-224:8; 5/7/19 Tr. 260:16-262:9; 5/8/19 Tr. 180:14-184:2].

28. Because Taxpayer did not complete the requested subsidiary business connection questionnaires by the March 18, 2017, deadline, the Department proceeded with its assessment without the benefit of review of the information in those requested questionnaires.

29. On August 11, 2017, after Taxpayer already had filed its protest, Protest Auditor Mary Griego sought additional information about Taxpayer's percentage of ownership in each

[2] In the interest of efficiency and to reduce repetition, all the findings of fact contained in this general evidence of unitariness section apply to all of Taxpayer's 15 foreign subsidiaries except for Oil Insurance Limited and except when otherwise expressly noted when addressing the individual entities.

foreign subsidiary, documentation of the amounts of dividends paid by the entities, and additional information to substantiate the claimed oil and gas withholdings listed on the original return. [Dept. Ex. AI; 5/8/19 Tr. 187:3-189:12; 191:17-193:7].

30. In June of 2018, Taxpayer finally submitted the subsidiary business connection questionnaires the Department had previously requested on February 13, 2017 (before issuance of the assessment) and August 11, 2017 (Mary Griego's protest office request). [Dept. Ex. AH; Dept. Ex. AI; 5/8/19 Tr. 191:17-193:7].

31. While the Department only requested that Taxpayer complete subsidiary business questionnaires for five entities, Mr. Sauer, C.P.A., confirmed that the answers to the five subsidiary business questionnaires and his answers during his testimony generally applied to, and were substantially, similar to the remaining nine foreign subsidiaries (with some limited exceptions). [5/7/19 Tr. 188:25-201:9; 303:19-305:19].

32. In her role as protest auditor, Mary Griego extensively reviewed the subsidiary business connection questionnaires and other pertinent corporate documentation to consider whether Taxpayer's foreign subsidiaries were unitary businesses.

33. As part of that review, Mary Griego learned that Taxpayer's historic corporate ethos was of accelerating growth and acquisition of assets that can assist that growth in the oil and gas business. Taxpayer exhibited this philosophy when it acquired assets in Western Australia and in Canada. [Dept. Ex. C (12); 5/8/19 Tr. 218:15-216:11].

34. Taxpayer applied its corporate strategy and system to its acquired corporate entities to further its corporate goal of growth, both for Taxpayer and the acquired entity. [Dept. Ex. C (1-7); 5/8/19 Tr. 212:1-219:23].

35. Taxpayer's Human Resources Department reviewed each subsidiaries policy and salary guidelines. [Dept. Ex. AB-9; 5/7/19 Tr. 269:14-272:12].

36. Taxpayer provided a global employee code of conduct that applied to all subsidiaries. [5/7/19 Tr. 272:13-272:20].

37. Each entity managed its daily operations from its location with infrequent input from Taxpayer.

38. Taxpayer reported that it treated all operations, including all international and domestic subsidiaries, as one segment of business in its 10K Forms filed with the S.E.C. in 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2002, 2003, 2004, 2005, 2007, 2008, 2010, 2011, 2012, 2013, 2014, and 2015. [Dept. Ex. F-AA; 5/8/19 Tr. 236:10-239:4].

39. Taxpayer reported to the S.E.C. that its foreign earnings were permanently reinvested abroad rather than have dividends paid out in its 10K Forms filed in 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2002, 2003, 2004, 2005, 2007, 2008, 2010, 2011, 2012, 2013, and 2014. [Dept. Ex. F-AA; 5/8/19 Tr. 239:6-244:4].

40. Taxpayer's 2015 foreign dividends represented accrual of deferred earnings over 23-years, as reported in Taxpayer's 10K filings with the S.E.C. [Dept. Ex. F-AA; 5/8/19 Tr. 239:6-251:5].

41. Taxpayer used the foreign earnings from the foreign subsidiaries to fund international operations rather than have those earnings paid out as dividends. [Dept. Ex. F-AA; 5/9/19 Tr. 74:2-75:7].

42. After reviewing the 10K Forms filed by Taxpayer, all the subsidiary business connection questionnaires, other corporate materials, the Department's Corporate Income Tax Audit Manual, and listening to the testimony of Mr. Sauer during the hearing, Protest Auditor

Mary Griego formed the opinion that Taxpayer's foreign subsidiaries at issue in this protest were all unitary businesses with Taxpayer. No one factor dictated this conclusion, but Ms. Griego considered numerous factors and concluded that Taxpayer's acquisition of the foreign subsidiaries led to functional integration, centralization of management, and economies of scale in employing Taxpayer's oil and gas production system, reducing administrative costs, employee costs, and reducing other costs. Ms. Griego concluded that Taxpayer and the foreign subsidiaries were all in the same line of business of oil and gas production and that Taxpayer dictated the major operational and business decisions of the subsidiaries. [Dept. Ex. C (1-19); 5/8/19 Tr. 212:1-227:23; 272:3-273:18; 5/9/19 T; r. 41:2-42:17].

b. Apache Energy Limited's Unitariness

43. Apache Energy Limited is an Australian oil and gas exploration and production company formed in 1991. Taxpayer acquired the entity from a third party in 1993. Apache Energy Limited served as the parent entity of numerous subsidiaries operating in Australia. [Taxpayer Ex. #17; 5/7/19 Tr. 62:13-63:5; 77:11-80; 106:1-9; 175:14-175:23; 209:1-209:13; 5/8/19 Tr. 82:22-83:2].

44. In its 1993 purchase, Taxpayer intended to expand its oil and natural gas interests in Australia by merging operations with the acquired entity. [Dept. Ex. E; 5/8/19 Tr. 231:10-232:15].

45. Taxpayer shared common officers and directors with Apache Energy Limited. [Taxpayer Ex. #17; 5/7/19 Tr. 176:11-176:20].

46. Apache Energy Limited's daily operations were managed out of Perth, Australia with infrequent input from Taxpayer. Taxpayer approved annual budgets for Apache Energy Limited and its subsidiaries, approved capital expenditures greater than $10,000,000.00,

approved any possible mergers and acquisitions, approved any possible payment of dividends, provided oil sales marketing, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 176:20-182:20].

47. In general, Apache Energy Limited was a self-funding operation with any needed cash coming from Egypt or the United Kingdom. [Taxpayer Ex. #17; 5/7/19 Tr. 176:3-176:6].

48. However, in its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported its investment of $257,561,009.00 at the end of the reporting period as an asset for Apache Energy Limited. [Taxpayer Ex.#3.3 & #3.13].

c. Apache Lowendal Pty Limited's Unitariness

49. Apache Lowendal Pty Limited is another Australian oil and gas exploration company but without any subsidiaries. [5/7/19 Tr. 63:6-15].

50. Taxpayer approved Apache Lowendal Pty Limited's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

51. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported as an asset for Apache Lowendal Pty Ltd. $69,674,091.00 in intercompany receivables at the beginning and $30,509,538.00 at the end of the reporting period. [Taxpayer Ex. #2.1447 & #2.1454-1455].

d. Apache UK Limited's Unitariness

52. Apache UK Limited was a holding company with zero book income in 2015. [Taxpayer Ex. #15.3; 5/7/19 Tr. 63:16-24; 87:23-88:3].

53. Taxpayer approved Apache UK Limited's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, provided oil and gas marketing, approved any possible payment of dividends, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

54. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported its investment of $27,039,055.00 at the beginning and zero at the end of the reporting period as an asset for Apache UK Limited. [Taxpayer Ex.#2.1602, #2.1608].

e. Apache Australia Management General Partnership's Unitariness

55. Apache Australia Management General Partnership is a financing entity that financed Australian oil and gas exploration and production. This entity also had other subsidiaries. [5/7/19 Tr. 64:1-12].

56. Taxpayer approved Australia Management General Partnership's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

57. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported its investment of $278,274,404.00 at the beginning and zero at the end of the reporting period as an asset for Australia Management General Partnership. [Taxpayer Ex.#2.751, #2.758].

f. Apache Australia Management Finance General Partnership's Unitariness

58. Apache Australia Management Finance General Partnership is another financing entity that financed Australian oil and gas exploration and production. This entity also had other subsidiaries. [5/7/19 Tr. 64:13-23].

59. Taxpayer approved Apache Australia Management Finance General Partnership's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

g. Apache Canada Funding I Limited Partnership's Unitariness

60. Apache Canada Funding I Limited Partnership is a financing entity that financed Egyptian oil and gas exploration and production. [5/7/19 Tr. 64:24-65-13].

61. Taxpayer approved Apache Canada Funding I Limited Partnership's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

h. Apache Canada Funding III Limited Partnership's Unitariness

62. Apache Canada Funding III Limited Partnership is another financing entity that financed Egyptian oil and gas exploration and production. [5/7/19 Tr. 65:14-21].

63. Taxpayer approved Apache Canada Funding III Limited Partnership's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

64. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported as an asset for Apache Canada Funding III Limited Partnership $2,676,291,780.00 in intercompany receivables at the beginning and $1,934,699,221.00 at the end of the reporting period. [Taxpayer Ex. #2.811 & #2.815-816].

i. Apache Egypt Investment Corporation LDC's Unitariness

65. Apache Egypt Investment Corporation LDC served as a general partner in a partnership with Sinopec in Egypt. [5/7/19 Tr. 65:22-66:11].

66. Taxpayer approved Apache Egypt Investment Corporation LDC's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, provided oil sales marketing, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

67. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported its investment of $7,861,971.00 at the beginning and negative $3,165,815,851.00 at the end of the reporting period as assets of Apache Egypt Investment Corporation LDC. [Taxpayer Ex.#2.1050, #2.1054-1055].

j. Apache Finance Egypt I S.a.r.l.'s Unitariness

68. Apache Finance Egypt I S.a.r.l. served as a holding company for oil and gas operations in Egypt and Canada. [5/7/19 Tr. 66:12-18, 69:20-70:16].

69. Taxpayer approved Apache Finance Egypt I S.a.r.l.'s annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, provided oil sales marketing, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

70. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported its investment of $3,580,555,370.00 at the beginning and $1,115,165,195.00 at the end of the reporting period as assets of Apache Finance Egypt I S.a.r.l. [Taxpayer Ex.#3.25, #3.30-3.31].

k. Apache Egypt Holdings III Corporation LDC's Unitariness

71. Apache Egypt Holdings III Corporation LDC served as a holding company for oil and gas operations in Egypt. [5/7/19 Tr. 67:1-13].

72. Taxpayer approved Apache Egypt Holdings III Corporation LDC's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, provided oil sales

marketing, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

73. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported its investment of $349,151,939.00 at the beginning and $91,021,389.00 at the end of the reporting period as assets of Apache Egypt Holdings III Corporation LDC. [Taxpayer Ex.#3.55, #3.60-3.61].

l. Apache Egypt Holdings IV Corporation LDC's Unitariness

74. Taxpayer formed Apache Egypt Holdings IV Corporation LDC to serve as a holding company for certain Egyptian operating entities. [Taxpayer Ex. #17; 5/7/19 Tr. 67:14-19; 182:21-183:3].

75. Apache Egypt Holdings IV Corporation LDC was a self-funding entity. [Taxpayer Ex. #17; 5/7/19 Tr. 183:4-183:12].

76. Apache Egypt Holdings IV Corporation LDC's daily operations were managed out of Luxembourg with infrequent input from Taxpayer. However, Taxpayer approved annual budgets for Apache Egypt Holdings IV Corporation LDC, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, provided oil sales marketing, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:24-192:13].

77. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported its investment of $5,180,888,069.00 at the beginning and

$2,158,748,385.00 at the end of the reporting period as assets of Apache Egypt Holdings IV Corporation LDC. [Taxpayer Ex.#2.1040, #2.1044-1045].

m. Apache Asyout Corporation LDC's Unitariness

78. Apache Asyout Corporation LDC is an Egyptian oil and gas company. [5/7/19 Tr. 68:5-13].

79. Taxpayer approved Apache Asyout Corporation LDC's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, provided oil and gas marketing, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

80. In its 2015 Form 5471, Schedule F with supporting documentation, filings with the IRS, Taxpayer reported as an asset for Apache Asyout Corporation LDC $4,630,351.00 in intercompany receivables at the beginning of the reporting period. [Taxpayer Ex. #2.713 & #2.719].

n. Apache International Holdings S.a.r.l.'s Unitariness

81. Apache International Holdings S.a.r.l. was originally formed as a holding company. It served as the parent company of several subsidiaries in the United Kingdom and Australia that were purchased from third parties. [Taxpayer Ex. #17; 5/7/19 Tr. 68:14-20; 165:18-166:3].

82. Taxpayer shared common officers and directors with Apache International Holdings S.a.r.l. [Taxpayer Ex. #17; 5/7/19 Tr. 166:22-167:6].

83. Apache International Holdings S.a.r.l.'s daily operations were managed out of Luxembourg with infrequent input from Taxpayer. However, Taxpayer approved annual budgets for Apache International Holdings S.a.r.l. and its subsidiaries, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, provided oil sales marketing, transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 167:7-174:14].

84. Apache International Holdings S.a.r.l. was funded with excess cash from other operating regions and short term, arm's length loans from Taxpayer in the form of issuance of Taxpayer stock. [Taxpayer Ex. #17; Dept. Ex. A7; 5/7/19 Tr. 166:18-166:3; 5/8/19 Tr. 262:20-264:13].

85. Because Taxpayer funded the acquisition of Apache International Holdings S.a.r.l. through issuance of Taxpayer stock, the Department concluded that Apache International Holdings S.a.r.l. was unitary with Taxpayer and any dividends generated from Apache International Holdings S.a.r.l. were business income. [Taxpayer Ex. #17; Dept. Ex. A7; 5/8/19 Tr. 262:20-264:13].

o. Apache UK Corporation LDC's Unitariness

86. Apache UK Corporation LDC is a holding company for United Kingdom oil and gas operations. [5/7/19 Tr. 68:21-69:1].

87. Taxpayer approved Apache UK Corporation LDC's annual budget, approved capital expenditures greater than $10,000,000.00, approved any possible mergers and acquisitions, approved any possible payment of dividends, provided oil and gas marketing,

transferred limited amount of personnel between entities, shared a common internal audit function, maintained common charts of accounts to facilitate S.E.C. filings, shared liability insurance, and shared a common logo. [Taxpayer Ex. #17; 5/7/19 Tr. 188:25-201:9].

p. Oil Insurance Limited's Lack of Unitariness

88. Oil Insurance Limited is an insurance co-op which insures oil and gas companies that operate in the Gulf of Mexico from windstorms, hurricanes, and other types of naturally occurring destructive events. [5/7/19 Tr. 69:2-22].

89. Taxpayer owns less than a 5% stake in Oil Insurance Limited. [5/7/19 Tr. 69:2-22].

90. The remaining owners of Oil Insurance Limited are also oil and gas companies that operate in the Gulf of Mexico, all of whom are unrelated by ownership with Taxpayer. [5/7/19 Tr. 69:2-20].

91. There was little evidence presented about the extent of Taxpayer's role in the operations, management, or control of Oil Insurance Limited and the general unitariness findings of fact do not apply to this entity.

92. Taxpayer has no officers or directors on the board of Oil Insurance Limited, shares no administrative or management functions with Oil Insurance Limited, and Oil Insurance Limited serves no function to Taxpayer other than providing insurance. [5/7/19 Tr. 192:19-193:17].

93. Oil Insurance Limited generated $18,588,489.00 of Taxpayer's 2015 foreign dividends. [Taxpayer Ex. #15.1].

Taxpayer's Strategic Rebalancing

94. Beginning in late 2012, Taxpayer made a strategic decision to rebalance its global operations away from its foreign subsidiaries towards North America. This strategic rebalancing led Taxpayer to sell off a third of its assets in Egypt, sell all of its Argentina operations in 2014, and sell off all of its Australia operations in 2015. [5/7/19 Tr. 47:20-48:9; 201:23-202:20].

95. In May of 2013, Taxpayer announced its plans to divest itself of approximately $4,000,000,000.00 in foreign subsidiary assets and use the proceeds of that sale to pay down debt and repurchase Taxpayer common shares. Taxpayer exceeded these goals in selling the assets, divesting itself of approximately $7,000,000,000.00 in assets, shredding $2,600,000,000.00 of debt, and repurchasing one billion dollars of outstanding shares. [Dept. Ex. Y.4; 5/8/19 Tr. 251:8-253:16].

96. The purpose of Taxpayer's strategic divestment was to increase cash flow from international operations and to enhance Taxpayer's North American portfolio with its more predictable rate of return. [Dept. Ex. Y.4; Dept. Ex. Z.4].

97. In 2013, Taxpayer sold a one third interest in a general partnership in its Egyptian operations to Sinopac, a Chinese oil and gas company. [Taxpayer Ex. #18.2; 5/7/19 Tr. 47:23-48:5; 202:2-7; 203:11-13; 204:4-6].

98. Between 2013 through 2015, Taxpayer sold portions of its operations in Western Canada, including certain assets and all its stock in several Canadian operating entities. [Taxpayer Ex. #16; Taxpayer Ex. #18.2; 5/7/19 Tr. 47:23-48:9; 204:7-9].

99. Between 2013 and 2015, Taxpayer also disposed of significant portions of its operations in the Gulf of Mexico. [Taxpayer Ex. #16; Taxpayer Ex. #18.2; 5/7/19 Tr. 47:23-48:9; 204:7-9].

100. In 2014, Taxpayer sold all its shares in Argentinian companies, ceasing all operations in Argentina. [Taxpayer Ex. #16; 5/7/19 Tr. 204:10-204:14].

101. In 2015, Taxpayer sold all its shares in its Australian parent company, Apache Energy Limited, ceasing all operations in Australia. [Taxpayer Ex. #16; 5/7/19 Tr. 206:15-206:22].

102. Based on Mr. Sauer's best unconfirmed estimate, Taxpayer generated approximately $3,000,000,000.00 in income from the sale of one third of its Egyptian operations and the entirety of its Australian and Argentinian operations. [5/7/19 Tr. 263:3-265:2].

103. Taxpayer's decision to strategically rebalance its global operations was the first and only time it had undertaken such a rebalancing. [5/7/19 Tr. 48:10-21; 206:23-207:5].

Taxpayer's New Mexico Operations in the Permian Basin

104. In New Mexico, Taxpayer performs petroleum and natural gas exploration and production but does not perform other centralized functions within the state. [5/7/19 Tr. 36:16-37:1].

105. Taxpayer and the following six of its subsidiaries conducted business in New Mexico during the 2015 tax year: (a) Apache Marketing, Inc.; (b) Apache Permian Basin Corporation; (c) DEK Energy Company; (d) Edge Petroleum Exploration Company; (e) Apache Deepwater LLC; and (f) Texas and New Mexico Exploration LLC. [Taxpayer Ex. #1.1-1.2; 5/9/19 Tr. 89:9-90:2].

106. The seven entities that were part of Taxpayer's domestic group that did business in New Mexico had a taxable loss in 2015 of approximately $10,000,000.00. [5/9/19 Tr. 90:3-90:10].

107. Between 1991 and 2015, when the unitary foreign subsidiaries were acquired and began accumulating the disputed deferred dividend income, the Permian Basin, encompassing portions of Texas and New Mexico, was an important region in Taxpayer's oil and gas production business. [Dept. Ex. F.002; Dept. Ex. G.002; Dept. Ex. H.002; Dept. Ex. I.002; Dept. Ex. J.002; Dept. Ex. K.002; Dept. Ex. L.002; Dept. Ex. N.002; Dept. Ex. O.002; Dept. Ex. P.002; Dept. Ex. Q.002; Dept. Ex. S.002; Dept. Ex. T.002; and Dept. Ex. V.002; Taxpayer Ex. Z.0019; Dept. Ex. Y.0018; Dept. Ex. AA.0015; Dept. Ex. C.7-17, 30; 5/8/19 Tr. 217:18-218:7].

108. In 1991, Taxpayer acquired MW Petroleum, with wells located in the Permian Basin of West Texas and New Mexico. This acquisition of MW Petroleum in 1991, including the assets in the Permian Basin, doubled Taxpayer's size and pushed Taxpayer's assets above $1,000,000,000.00. [Dept. Ex. C.7, C.26-30; 5/8/19 Tr. 217:18-218:7].

109. By the end of 1991, Taxpayer's greatest concentration of properties were located along the Gulf Coast and in the Permian Basin of West Texas and New Mexico, where Taxpayer held a controlling interest in over 1,000 operating wells. Taxpayer highlighted its focus on the Permian Basin, along with two or three other regions, in North America, in its filings with the S.E.C. in 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2002, 2003, 2004, 2005, 2007, 2008, and 2010. [Dept. Ex. C.30; Dept. Ex. F.002; Dept. Ex. G.002; Dept. Ex. H.002; Dept. Ex. I.002; Dept. Ex. J.002; Dept. Ex. K.002; Dept. Ex. L.002; Dept. Ex. N.002; Dept. Ex. O.002; Dept. Ex. P.002; Dept. Ex. Q.002; Dept. Ex. S.002; Dept. Ex. T.002; and Dept. Ex. V.002].

110. In 2013, 2014, and 2015, Taxpayer's North American oil and gas exploration and production activities occurred primarily in the Permian Basin of West Texas and New Mexico, the Anadarko Basin in Oklahoma and Texas, and along the U.S. coast of the Gulf of Mexico. During that same time frame, Taxpayer's international oil and gas exploration and production

activities occurred in Argentina, Australia, Canada, Egypt, and the United Kingdom (North Sea). [Taxpayer Ex. #18.1 (¶6); Dept. Ex. AA; 5/7/19 Tr. 37:2-7].

111. In 2013 and 2014, during the period when Taxpayer was strategically rebalancing its assets and business operations towards North America, the Permian Basin played a central role in Taxpayer's total liquid worldwide production and growth. In 2013, Taxpayer noted that its focused drilling program in the Permian and Anadarko Basins provided momentum to Taxpayer's production growth in the United States. In 2014, Taxpayer's Permian Basin liquid production, amounting to just under a third of all global production, led Taxpayer's total worldwide liquid production. [Taxpayer Ex. Z.0019; Dept. Ex. Y.0018].

112. In 2015, Taxpayer operated an average of 12 rigs in the Permian Basin, drilling 378 gross wells and 241 net wells. [Dept. Ex. AA.0015].

113. Taxpayer's 2015 drilling activity in the Permian Basin resulted in a production increase of 6 percent relative to 2014. [Dept. Ex. AA.0015].

114. The Permian Basin's liquid production in 2015, which averaged 168 MBOE/d[3], was more than double Taxpayer's production in any other North American production regions and was larger than production in any of Taxpayer's international production regions in 2015. [Dept. Ex. AA.0015].

115. In 2015, Taxpayer's Permian Basin operations formed the largest plurality of total worldwide liquid oil and gas production, amounting to more than a third of Taxpayer's total liquid production in that year. [Dept. Ex. AA.0015].

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[3] MBOE/d means thousand barrels of oil equivalent per day. *See Camelot Event Driven Fund v. Alta Mesa Res.*, Inc., 2021 WL 1416025, at *3 (S.D. Tex. Apr. 14, 2021) (non-precedential, cited simply to provide definition of that abbreviation).

Taxpayer's 2015 Income, Federal, and State Corporate Income Tax Returns

116. Mr. Sauer prepared and filed Taxpayer's original 2015 CIT-1120 U.S. Corporation Income Tax Return. [Taxpayer Ex. #2; 5/7/19 Tr. 49:3-6, 52:13-53:23].

117. In 2015, Taxpayer reported $24,819,786,617.00 in total income before deductions. [Taxpayer Ex. #2.1(line 11); 5/7/19 Tr. 50:2-5].

118. In 2015, Taxpayer reported $19,431,277,375.00 in federal taxable income before deductions for net operating losses. [Taxpayer Ex. #2.1(line 28); 5/7/19 Tr. 95:11-96:8].

119. In 2015, Taxpayer reported $19,337,993,126.00 in federal taxable income after a deduction of $93,284,249.00 for net operating losses. [Taxpayer Ex. #2.1(lines 28-30); 5/7/19 Tr. 50:22-51:7].

120. In 2015, Taxpayer reported $22,046,265,838.00 in total dividends, of which $45,576.00 came from U.S. dividends while the remaining $22,046,219,262.00 came from foreign dividends. [Taxpayer Ex. #2.2(line 17 & 19); 5/7/19 Tr. 49:10-51:3].

121. In 2015, Taxpayer reported $8,529,941,448.00 in foreign dividend gross-up. [Taxpayer Ex. #2.2(line 15); Taxpayer Ex. #1.3; 5/7/19 Tr. 50:22-51:7].

122. Taxpayer calculated an average apportionment factor in New Mexico of 5.7911% on its original 2015 CIT-1 return. [Taxpayer Ex. #1.4(line 9); 5/7/19 Tr. 99:18-22; 5/8/19 Tr. 47:18-48:2].

123. As part of calculating the average apportionment factor in 2015, on its original CIT-1 return, Taxpayer identified $4,035,815,376.00 in total New Mexico property, $7,920,644.00 in New Mexico payroll, and $383,428,588 in New Mexico sales. [Taxpayer Ex. #1.4; 5/8/19 Tr. 52:20-53:7].

124. Taxpayer's calculated 2015 average apportionment factor in New Mexico on its original CIT-1 return did not include property, payroll, or sales factors from the income-paying foreign subsidiaries. [Taxpayer Ex. #1.4; 5/7/19 Tr. 99:23-100:3].

125. Despite calculating a New Mexico factor of 5.7911%, Taxpayer originally reported 0% as its New Mexico percentage factor for purposes of apportionment on its original 2015 CIT-1. [Taxpayer Ex. #1.3(line 11); Taxpayer Ex. #1.4; Taxpayer Ex. #1.5; 5/8/19 Tr. 46:10-52:20].

126. Taxpayer claimed the New Mexico deduction for its foreign dividend gross-up of $8,529,941,448.00, leaving $13,497,689,325.00 of foreign dividends in dispute in this protest. [Taxpayer Ex. #1.5; 5/7/19 Tr. 56:6-17; 5/7/19 Tr. 96:14-97:15].

127. Of the remaining, disputed $13,497,689,325.00 of foreign dividends, $2,436,945,549.00 was Subpart F income. [Taxpayer Ex. #15.3 (Column Subpart F & 956); 5/7/19 Tr. 70:20-73:16; 208:11-208:19].

128. Of the disputed $13,497,689,325.00 of foreign dividends, $4,621,665,875.00 was attributable to a check-the-box election. [Taxpayer Ex. #15.3 (Column Actual, Apache UK Limited + Apache International Holdings S.a.r.l.); 5/7/19 Tr. 73:23-77:7; 208:20-208:24].

129. The two entities that reported income attributable to the check-the-box election on federal Form 8832 were Apache International Holdings S.a.r.l. and Apache UK Limited. [5/7/19 Tr. 211:19-212:20].

130. Taxpayer estimated that about 76% of the disputed $13,497,689,325.00 of foreign dividends was attributable to earnings and profits accumulated over multiple previous years before 2015, dating back as far as 1991 to the formation of Apache Energy Limited. [5/7/19 Tr. 77:11-80; 106:1-9; 209:1-209:13; 5/8/19 Tr. 82:22-83:2].

131. Five of the fifteen entities that reported foreign dividends or Subpart F income in tax year 2015 had no book income or negative book income in 2015:

a. Apache Energy Limited, which had negative book income in 2015 because of US GAAP-related required write-downs;

b. Apache UK Limited, which had zero book income in 2015, as it was merely a holding company;

c. Apache Egypt Holdings IV Corporation LDC, which had negative book income in 2015 because of a minor loss of interest expense it occurred;

d. Apache Asyout Corporation LDC, which had zero book income in 2015 because it was an inactive company;

e. Apache UK Corporation LDC, which had negative book income in 2015 because of US GAAP-related required write-downs.

[Taxpayer Ex. #15.3; 5/7/19 Tr. 82:11-87:15].

132. Despite having no book income or negative book income, these five entities listed in the previous finding of fact did generate real income totaling $3,362,577,203.00 in tax year 2015. [Taxpayer Ex. #15.3; 5/7/19 Tr. 87:23-88:3].

133. Taxpayer paid foreign taxes totaling over one billion dollars on its 2015 foreign source dividend income. [5/7/19 Tr. 219:2-219:8].

134. Taxpayer received a federal foreign tax credit in 2015 for the foreign taxes it paid. [Taxpayer Ex. #2; 5/7/19 Tr. 219:9-219:12].

135. Taxpayer did not receive any credit in New Mexico for the 2015 foreign taxes it paid. [Taxpayer Ex. #1; 5/7/19 Tr. 219:13-219:16].

136. All the dividends at issue in this case were paid by Taxpayer's subsidiaries. [5/8/19 Tr. 10:20-11:3].

137. Taxpayer reported the dividend income as non-business income on federal Form 1120 because Taxpayer considered that income non-unitary and non-business income. Since there was no line on the form to report non-unitary income, Taxpayer reported the dividend income as non-business income on Form 1120. [Taxpayer Ex. #2; 5/8/19 Tr. 18:4-19:7].

138. Taxpayer's original CIT-1 return claimed a $19,422,282.00 refund of 2015 New Mexico corporate income taxes. [Taxpayer Ex. #1.3 (line 29); 5/6/19 Tr. 203:3-21].

Department Review of the CIT-1 Return, Return Adjustment Notices, and Assessment

139. On January 28, 2017, the Department issued Taxpayer a Return Adjustment Notice (Refund Due), showing a minor reduction of $50,775.00 in the $19,422,282.00 refund amount that Taxpayer had claimed on the original 2015 CIT-1 return. [Taxpayer Ex. #5; Taxpayer Ex. #1.3; 5/6/19 Tr. 203:3-21].

140. Taxpayer entered the information requested by the January 28, 2017, Return Adjustment Notice to facilitate direct deposit of the refund. [Taxpayer Ex. #5.1; 5/6/19 Tr. 203:12-21].

141. At some unspecified time between the January 28, 2017, Return Adjustment Notice and February 13, 2017, someone in the Department's corporate income audit unit asked Corporate Auditor Mr. Armer about requesting additional documentation from Taxpayer about how the foreign dividends were allocated. [Dept. Ex. AH; 5/8/19 Tr. 70:5-70:12; 71:18-21; 144:12-149:8].

142. On February 13, 2017, the Department mailed a document titled "Request for Additional Information" to Taxpayer at 2000 Post Oak Blvd STE 100, Houston, TX 77056-4400.

This letter was addressed to the same address that Taxpayer listed on its 2015 CIT-1 return. [Dept. Ex. AH; Taxpayer Ex. #1.1 (lines 1a through 3a); 5/6/19 Tr. 223:9-224:8; 5/7/19 Tr. 260:16-262:9; 5/8/19 Tr. 180:14-184:2].

143. The Department's February 13, 2017, "Request for Additional Information" asked that Taxpayer provide additional information to verify the refund claim, and specifically requested a completed copy of Taxpayer's Form 1120 Schedule C and completion of the "Foreign Dividend and Subpart F Income Payor Business Connection Questionnaire" by March 18, 2017. [Dept. Ex. AH; 5/6/19 Tr. 223:9-224:8; 5/7/19 Tr. 260:16-262:9; 5/8/19 Tr. 180:14-184:2].

144. The Department did not receive the requested additional information before issuance of the assessment. [5/8/19 Tr. 72:21-73:1].

145. The Department conducted no formal audit in this matter before issuing its assessment. [5/8/19 Tr. 70:5-70:12; 71:14-17; 72:10-72:12; 73:2-73:6].

146. Without receiving the requested additional information or conducting a formal audit, the Department proceeded with the assessment based on the information Taxpayer provided on the original CIT-1 return. [5/8/19 Tr. 72:21-73:1; 5/8/19 Tr. 187:3-196:1].

147. Given Taxpayer's actual 2015 New Mexico property, payroll, and sales, the Department determined that Taxpayer's claim for 0% apportionment factor percentage in New Mexico was not reflective of its actual business activities in New Mexico during 2015, requested additional information from Taxpayer, and ultimately disallowed Taxpayer's claim for $13,497,689,325.00 in non-business income. [5/8/19 Tr. 53:8-54:3].

148. The Department applied the 5.79% apportionment factor calculated by Taxpayer against Taxpayer's reported taxable income on line 10 of $752,179,179.00 to determine

Taxpayer's New Mexico corporate income tax due. [Taxpayer Ex. #1.3(line10 &11); 5/8/19 Tr. 53:7-55:23].

149. On March 21, 2017, the Department issued Taxpayer a Return Adjustment Notice (Proposed Assessment), showing a proposed total assessment of $43,559,798.00 in 2015 corporate income tax, $2,418,744.10 in penalty, and $947,590.37 in interest, offset by credits totaling $19,372,357.00 for a total proposed assessment of $27,553,775.47. [Taxpayer Ex. #6; 5/6/19 Tr. 204:2-19].

150. The Department's March 21, 2017, Return Adjustment Notice cited three specific reasons for the proposed assessment: 1) "CIT-1 line 11. Error in computing NM Percent;" 2) "CIT-1 line 11. Allocation and apportionment factors are to calculate tax percentage, not taxable income;" and 3) "CIT-1 line 12. Tax adjusted. Schedule CC not attached." [Taxpayer Ex. #6.2; 5/6/19 Tr. 205:13-206:4].

151. Mr. Sauer was uncertain whether any of his staff attempted to call the Department to discuss the March 21, 2017, Return Adjustment Notice showing a substantial proposed assessment. [5/6/19 Tr. 224:9-19].

152. Corporate Income Auditor Mr. Armer and Protest Auditor Mary Griego were unaware what communications, if any, occurred between the Department and Taxpayer before the Department issued its assessment. [5/8/19 Tr. 73:13-75:21; 196:12-197:11].

153. The Department's information technology system, Gentax, does not show any calls or contact from Taxpayer before issuance of the assessment. [5/8/19 Tr. 196:17-197:11].

154. Corporate Income Auditor Mr. Armer recognized that there was a substantial swing between the Department's initial Return Adjustment Notice showing a potential Taxpayer refund of approximately $19,000,000.00 and the Department's subsequent assessment of

approximately $24,500,000.00, a difference of some $43,500,000.00. Mr. Armer believed best practice would have been to perform a detailed audit before making such a substantial adjustment, but Mr. Armer also recognized that in the absence of Taxpayer's response to the Department's request for additional information, the Department's revenue processing division had to proceed with an assessment based on the limited information they had been provided. [5/8/19 Tr. 75:22-81:7].

155. Mr. Sauer believed that the explanation on the March 21, 2017, Return Adjustment Notice (proposed assessment), and lack of subsequent explanation before the March 31, 2017, Notice of Assessment, was inadequate to support the adjustment from a refund due of some $19,000,000.00 to an assessment of some $24,500,000.00, especially compared to his experience with filings in other states. [5/6/19 Tr. 207:9-210:3].

156. On March 31, 2017, the Department issued the assessment in dispute in this matter, as described in more detail by F.O.F. #1. The assessed amount was $500 less than the proposed assessment contained on the Department's March 21, 2017, Return Adjustment Notice. [Taxpayer Ex. #7; 5/6/19 Tr. 206:12-23].

Original Apportionment Method Contained Obvious Distortion

157. Before the assessment, Taxpayer did not petition the Department for equitable allocation relief under NMSA 1978, Section 7-4-19. Specifically, Taxpayer did not seek permission to use the Section 965 concept (detailed later in these findings of fact) as a form of equitable relief, did not seek permission to file under a separate accounting method, did not seek application of the Detroit Formula, and did not file a petition for equitable relief with its original return. [5/8/19 Tr. 23:22-24:14; 56:21-60:6; 89:13-92:4].

158. In the absence of a petition for equitable relief and in the absence of the requested follow-up information, the Department relied on Taxpayer's CIT-1 reported average apportionment factor in New Mexico of 5.79% in calculating the assessment, and therefore did not provide any foreign factor relief in the apportionment ratio. [Taxpayer Ex. #1.4(line 9); Taxpayer Ex. #6.2; 5/7/19 Tr. 100:5-103:19; 5/8/19 Tr. 54:4-54:14].

159. Although Mr. Armer believed that the Department acted appropriately based on the original CIT-1 return and the Taxpayer's lack of response to the request for additional information before issuance of the assessment, he believed, based on the subsequent information received during the protest process and the evidence presented at the protest hearing, that there was "obvious distortion" resulting from application of the standard three-factor apportionment method used to calculate the original assessment. For the same reason, he believed that such obvious distortion needed to be corrected by an alternative, reasonable apportionment method. [5/8/19 Tr. 81:8-85:7; 104:10-23; 111:11-112:5].

160. Mr. Armer believed that, based on the substantial sum of foreign source income included in the New Mexico tax base, a more reasonable alternative apportionment method would be appropriate in this case, as permitted under UDITPA. [5/8/19 Tr. 82:6-85:7; 111:11-112:5].

Taxpayer's Proposed 965 Concept and Maine Alternative Apportionment Methods

161. In 2017, the federal Tax Cuts and Jobs Act (TCJA) passed Congress and was signed into law. Under this law, as of December 31, 2017, there was a deemed distribution and repatriation of all foreign earnings not previously remitted as foreign dividends in corporate income tax year 2017. Mechanically, this deemed repatriation was calculated using federal Form 965. [5/7/19 Tr. 103:20-106:22].

162. On January 1, 2019, in response to the deemed repatriation provisions of the TCJA, the Department issued a special bulletin and form, Department Bulletin B-300.17 and Form 2017 CIT-DFI, addressing the New Mexico treatment of Internal Revenue Code ("I.R.C. [4]") Section 965 untaxed foreign earnings in tax year 2017, as well as a new form, 2017 CIT-DFI for taxpayers with Section 965 income to report. [Taxpayer Ex. #14].

163. Corporate Income Tax Auditor Mr. Armer was part of the Department review team, which included Tax Policy, Legal Services, and Audit and Compliance, that developed the Department Bulletin B-300.17 and Form 2017 CIT-DFI addressing the New Mexico treatment of I.R.C. Section 965 untaxed foreign earnings in tax year 2017. [5/8/19 Tr. 64:10-66:21; 92:17-99:2].

164. As part of the development of Department Bulletin B-300.17 and Form 2017 CIT-DFI, the Department considered the merits of various other percentages of deductions used in other states to address the Section 965 income before settling on a 30% exclusion of the Section 965 income. [5/8/19 Tr. 64:10-66:21; 92:17-99:2].

165. For tax year 2017, under Department Bulletin B-300.17 and Form 2017 CIT-DFI, the Department permitted taxpayers to exclude 30% of their net I.R.C. Section 965 deferred foreign income from their taxable income in recognition of the fact that such income accrued over long periods before 2017 and the complexity of including foreign factors from an extended period would involve onerous recordkeeping to determine the appropriate apportionment. This 30% exclusion applied on line 6 of the Department's 2017 CIT-DFI Form. [Taxpayer Ex. #14.2 & #14.5].

[4] Citations to I.R.C. are also interchangeable with 26 U.S.C. As an example, I.R.C. § 1501 is also 26 U.S.C. § 1501. Under blue book citation, citation to the Internal Revenue Code are made using I.R.C. rather than 26 U.S.C. However, the appendix to NMRA 23-112 seem to suggest that the citation be to the United States Code, and thus 26 U.S.C. may also be referenced in this decision when referring to provisions of I.R.C.

166. During the development of Department Bulletin B-300.17 and Form 2017 CIT-DFI addressing the New Mexico treatment of I.R.C. Section 965 untaxed foreign earnings in tax year 2017, the Department believed and intended that the special bulletin and form would only apply to tax year 2017 and the TCJA's one-time deemed repatriation. [Taxpayer Ex. #14.1; 5/8/19 Tr. 64:10-66:21; 92:17-100:4].

167. Only taxpayers liable under Section 965 in 2017 or 2018 were expressly covered by the Department Bulletin B-300.17 and Form 2017 CIT-DFI. [Taxpayer Ex. #14; 5/8/19 Tr. 26:15-27:9].

168. Department Bulletin B-300.17 is only applicable to TCJA's 2017 deemed dividend repatriation: 1) "This bulletin applies only to taxpayers liable for New Mexico Corporate Income Tax who are required by Internal Revenue Code (IRC) Section 965 to pay a *transition tax* on the untaxed foreign earnings of certain foreign corporations. Generally, Section 965 requirements only apply to tax year 2017."; and 2) "This bulletin addresses only the changes to New Mexico taxable income pursuant to Section 14103 of the TCJA pertaining to a *one-time inclusion in tax year 2017* of certain untaxed foreign earnings and profits…" [Taxpayer Ex. #14.1, (emphasis added)].

169. Taxpayer believed that the Department's treatment of Section 965 income in 2017 was analogous to the 2015 foreign dividends at issue in this protest. [5/8/19 Tr. 26:9-26:14].

170. The Department did not believe that the Department's treatment of Section 965 income in 2017 was analogous to the 2015 foreign dividends at issue in this protest. The Section 965 concept was related specifically to the unique 2017 and 2018 repatriation of income mandated by the TCJA of all taxpayers who had not previously remitted the foreign income rather than to Taxpayer's voluntary election in 2015. [5/8/19 Tr. 106:5-107:24].

171. Taxpayer prepared a work paper showing the application of the Department's 2017 treatment of I.R.C. 965 income as shown on the Department's 2017 CIT-DFI Form, as well as Maine's 2017 80% exclusion treatment of I.R.C. 965 income, to Taxpayer's 2015 income. [Taxpayer Ex. #20; 5/7/19 Tr. 113:4-122:07].

172. Under Taxpayer's work paper showing the theoretical application of the Department's 2017 treatment of I.R.C. 965 income to Taxpayer's 2015 income, Taxpayer used an apportionment percentage of 4.9092% rather than the 5.79% Taxpayer reported on its 2015 return. [Taxpayer Ex. #20; 5/7/19 Tr. 117:1-119:18].

173. Under Taxpayer's work paper showing the theoretical application of the Department 2017 treatment of I.R.C. 965 income to Taxpayer's 2015 income, Taxpayer listed a deduction of $10,087,195,555.00 on the line §965(c). [Taxpayer Ex. #20; 5/8/19 Tr. 29:7-30:11; 5/8/19 Tr. 63:7-64:9].

174. The Department believed that Taxpayer's proposed deduction of $10,087,195,555.00 under the 965 concept came from Taxpayer's statement of repatriated income from the IRS Form 965. However, Auditor Mr. Armer did not believe that was analogous because IRS Form 965 applied only to income repatriated in 2017 and not to income repatriated in previous years. [Taxpayer Ex. #20; 55/8/19 Tr. 63:10-16].

175. Alternatively, Taxpayer believed that Maine's treatment of foreign dividends for state corporate income tax purposes was similar to New Mexico's approach, and thus Taxpayer also used Maine's 80% exclusion of the I.R.C. 965(a) amount in 2017 as a theoretical equitable adjustment to Taxpayer's 2015 income. [Taxpayer Ex. #20; 5/7/19 Tr. 120:1-121:14].

176. Under Taxpayer's work paper showing the theoretical application of Maine's 2017 treatment of I.R.C. 965 income to Taxpayer's 2015 income, Taxpayer used an apportionment

percentage of 4.8354% rather than the 5.79% Taxpayer reported on its 2015 return. [Taxpayer Ex. #20; 5/7/19 Tr. 120:1-122:7].

177. Neither of Taxpayer's proposed alternative apportionment methods resulted in a reasonable apportionment consistent with the economic reality that Taxpayer's operations in New Mexico's Permian Basin (before and during 2015) provided a substantial portion of Taxpayer's product in North America, deriving income before and during 2015. The income generated before 2015 helped Taxpayer acquire the foreign subsidiaries that generated the accumulated dividends in dispute. And the 2015 disposition helped further expand Taxpayer's unitary North American oil and gas operations, including further growth in New Mexico's Permian Basin.

Department Proposed Detroit and 30% Exclusion Alternative Apportionment Methods

178. Taxpayer also developed a work paper showing the application of the Detroit Formula to Taxpayer's 2015 income tax return, which resulted in reducing the apportionment factor from the reported 5.79% to 4.094%. Taxpayer did not prepare this work paper as an alternative apportionment method but to illustrate that the failure to provide foreign factor relief led to distortion. [Taxpayer Ex. #19; 5/7/19 Tr. 127:5-134:3].

179. Subject to review of Taxpayer's supporting documentation, the Department took Taxpayer's Detroit Formula workpaper and suggested[5] it as a potential alternative apportionment method in this case. [Administrative Record, Department Closing Argument, p. 24-26, 11/15/2019].

[5] It is unclear to the hearing officer whether in its closing argument that the Department was in fact offering the Detroit Formula as an alternative method or simply using it for distortive comparison analysis. However, at one point during the hearing, the Department's counsel said something to the effect that if Taxpayer was satisfied with the Detroit Formula, the Department would accept that as a reasonable alternative method and resolve the case on that basis. The written argument, in conjunction with the spirit of counsel's previous oral statement, supports a conclusion that the Department was offering the Detroit Formula as an alternative apportionment method in this protest.

180. Mr. Armer had concerns that the standard application of the Detroit Formula would not fairly prevent distortion in the unique circumstances of this case. In Mr. Armer's knowledge and experience, the Detroit Formula method worked better on a year-to-year basis rather than applied to an accumulation of dividends over many years. [5/8/19 Tr. 103:1-103:24; 106:19-107:3].

181. Based on the Department's working group review of the TCJA, Mr. Armer knew that the Department had determined that historically applying foreign factor relief yielded a 30% overall reduction in taxable income, which was a more effective method of addressing multiple years of accumulated dividends. [5/8/19 Tr. 65:14-66:21; 94:22-95:6; 112:08-23; 106:19-107:3; 113:24-115:14; 157:5-12].

182. To effectuate this 30% historical overall reduction in taxable income, Mr. Armer determined that a 30% exclusion of foreign dividend income was the appropriate method to apply to an accumulation of foreign dividends over many years but being reported in a single year. [Taxpayer Ex. #14; 5/8/19 Tr. 65:14-66:21; 94:22-95:6; 112:08-23; 106:19-107:3; 113:24-115:14; 157:5-12].

183. Although Mr. Armer disagreed with the application of the exact 965 concept and worksheet to Taxpayer's 2015 corporate income tax returns because the special bulletin and form only applied to tax year 2017, he did agree that a 30% overall exclusion in the accumulated foreign dividends in this case amounted to a fairer representation of Taxpayer's activities in New Mexico than either the standard apportionment method or the Detroit Formula. [Taxpayer Ex. #20; 5/8/19 Tr. 112:6-123:5].

184. To that end, as a potential reasonable alternative method, Mr. Armer prepared calculations applying the 30% New Mexico exclusion to Taxpayer's 2015 reported income. [Dept. Ex. AJ; 5/8/19 Tr. 156:6-156:13].

a. The line titled "CIT w/o FDE" represents Taxpayer's original 2015 CIT-1 taxable income without the foreign dividend amount of $13,502,111,901.00 [Dept. Ex. AJ; 5/8/19 Tr. 156:14-157:4];

b. The line titled "FDE" represents Taxpayer's foreign dividend amount of approximately $13,502,111,901.00 from Taxpayer's original 2015 CIT-1 taxable income [Dept. Ex. AJ; 5/8/19 Tr. 156:14-157:4];

c. The line titled "Less NM Exclusion 30% of FDE" represents Mr. Armer's attempt to effectuate factor representation by allowing a 30% exclusion of Taxpayer's $13,502,111,901.00 in foreign dividend income, which results in a subtraction of $4,050,633,570.00 [Dept. Ex. AJ; 5/8/19 Tr. 157:5-157:12];

d. The line titled "Less FTU" is the foreign gross-up deduction allowed by New Mexico, which in this case is $8,529,941,448.00 as taken from Taxpayer's original 2015 CIT-1 return [Dept. Ex. AJ; 5/8/19 Tr. 157:12-158:4];

e. The line titled "Sub" is the calculation so far on the form, showing $6,874,252,638.00 [Dept. Ex. AJ; 5/8/19 Tr. 157:23-158:4];

f. Using an average apportionment percent of 5.9711 in New Mexico taken from the original CIT-1 return, applying the tax rate to the subtotal amount, and crediting payments made, Mr. Armer's 30% exclusion method resulted in a tax due of approximately $13,694,412.00, subject to some possible minor adjustments related to withholding credits [Dept. Ex. AJ; 5/8/19 Tr. 158:5-159:18].

185. The Department's 30% exclusion method, based on historical analysis of foreign factor relief, is a reasonable alternative apportionment method that addressed the distortion present in this case while also being more consistent with the economic reality that Taxpayer's operations in New Mexico's Permian Basin provided a substantial portion of Taxpayer's product in 2015. This economic reality also existed in the years before 2015, when Taxpayer used the unitary income partially attributable to its important Permian Basin production to acquire the foreign subsidiaries and allowed the income to accumulate in the foreign subsidiaries rather than distribute the dividends.

Findings Related to other hearing issues, arguments, and objections

186. Taxpayer initially invoked the witness exclusion rule under Regulation 22.600.1.19 NMAC. The Department designated Protest Auditor Mary Griego as its case agent in the case, but also requested that Dan Armer be allowed to remain in the room as an expert witness. Although Mr. Armer had not been properly identified as an expert witness, the hearing officer ruled that Mr. Armer could remain in the hearing except when there was any testimony related to the business versus non-business income issue presented, which was to be the topic of Ms. Griego's testimony. After the first day of testimony, Taxpayer withdrew its invocation of the exclusionary rule except for requesting an instruction that Mr. Armer and Ms. Griego not discuss their testimony together during the proceeding. [5/6/19 Tr. 179:2-197:6:14-74:5; Tr. 5/7/19 40:14-42:10].

187. Taxpayer initially objected to the admission of Department Exhibit A, citing Rule of Evidence 11-408 NMRA prohibiting introduction of confidential disclosures made as part of settlement discussions. Taxpayer also included its own Exhibit #22, which it intended to offer as

a rebuttal to Department A, in its Rule 11-408 objection. However, Taxpayer ultimately withdrew this objection. [5/6/19 Tr. 61:14-74:5; 83:4-14; Tr. 5/7/19 26:7-20].

188. During the course of hearing, after Taxpayer had presented its case, the hearing officer ruled narrowly on the record that Taxpayer had met its initial burden of overcoming the presumption of correctness as to the assessed dollar amount of corporate income tax under the original assessment, leaving open the issue of what was an appropriate, alternative reasonable apportionment method. [5/8/21 Tr. 172:3-18; 173:16-174:3].

DISCUSSION

This protest involves seven main issues. The first issue is whether Taxpayer overcame the presumption of correctness on the original assessment and whether the Department in turn reestablished the correctness of the assessment. The second issue is whether the foreign subsidiaries at issue are unitary with Taxpayer. The third issue is whether Taxpayer's foreign dividend income, Subpart F income, and check-the-box deemed income constituted business or non-business income. The fourth issue is whether the Department's distinct treatment of foreign dividends unconstitutionally violates the Foreign Commerce Clause. The fifth issue is whether the Department's distinct treatment of foreign dividends unconstitutionally violates the Equal Protection Clause. The sixth issue considers whether the original assessment led to distortion of Taxpayer's 2015 New Mexico business activities and what is the most reasonable and appropriate alternative apportionment consistent with the economic reality of Taxpayer's 2015 New Mexico business activities. The seventh issue is whether Taxpayer is entitled to abatement of penalty in this protest. And finally, there are few other evidentiary issues, objections, and arguments requiring a brief discussion.

Issue One: Presumption of Correctness and Shifting of Burden

Under NMSA 1978, Section 7-1-17 (C) (2007), the assessment issued in this case is presumed correct. Consequently, Taxpayer has the burden to overcome the assessment. *See Archuleta v. O'Cheskey*, 1972-NMCA-165, ¶11, 84 N.M. 428. *See also N.M. Taxation & Revenue Dep't v. Casias Trucking*, 2014-NMCA-099, ¶8. Unless otherwise specified, for the purposes of the Tax Administration Act, "tax" is defined to include interest and civil penalty. *See* NMSA 1978, §7-1-3 (X) (2013). Under Regulation 3.1.6.13 NMAC, the presumption of correctness under Section 7-1-17 (C) extends to the Department's assessment of penalty and interest. *See Chevron U.S.A., Inc. v. State ex rel. Dep't of Taxation & Revenue*, 2006-NMCA-50, ¶16, 139 N.M. 498, 503 (agency regulations interpreting a statute are presumed proper and are to be given substantial weight). Accordingly, it is Taxpayer's burden to present some countervailing evidence or legal argument to show that they are entitled to an abatement, in full or in part, of the assessment issued in the protest. *See Casias Trucking*, 2014-NMCA-099, ¶8.

When a taxpayer presents sufficient evidence to rebut the presumption, the burden shifts to the Department to show that the assessment is correct. *See MPC Ltd. v. N.M. Taxation & Revenue Dep't*, 2003-NMCA-21, ¶13, 133 N.M. 217. In this case, the hearing officer on the record found that the Taxpayer had met its initial burden of showing that the original assessed dollar amount was not correct. This was a narrow ruling, focused on whether the dollar amount assessed accurately reflected a "reasonable approximation of the income earned in New Mexico.[6]" The Department's original assessed amount of tax was incorrect because the Department had to proceed to assessment based on the limited information contained in Taxpayer's original CIT-1 return after Taxpayer did not provide the additional, requested information to the Department.

[6] 5/8/21 Tr. 172:3-18; 173:16-174:3.

The biggest impact of finding that the burden shifted is evident in the discussion of whether the standard apportionment—which led to the original assessment—was in fact distortive. While the Department does make a few arguments defending the standard apportionment in its closing arguments—mainly that Taxpayer should be stuck with the standard apportionment method because of its failure to provide the additional, requested information or cooperate to the Department's satisfaction in the protest process—the Department essentially conceded in testimony and in closing argument that the standard apportionment method in this case resulted in obvious distortion that needed some correction. Consequently, in light of the shifting of the burden as to the correctness of the assessed amount and in light of the Department's concession of the obvious distortion, the distortion analysis in this decision will be quite minimal.

However, rebutting the presumption of correctness in this case has no impact on the question of what the reasonable alternative apportionment method is, given the case law in that area requiring the party advocating for an alternative method to demonstrate that the method is reasonable. And contrary to Taxpayer's argument, the hearing officer made no presumption of correctness ruling on the question of unitary business relationship and the case law (addressed in the unitary section) clearly puts the onus on Taxpayer to establish that the state is attempting to tax extraterritorial value regardless of the statutory presumption of correctness.

Issue Two: Taxpayer is Unitary with 14 of the 15 Foreign Subsidiaries.

In this case, Taxpayer argues that under both the plain statutory definition of unitary corporations and the three unity tests, the Department fails to establish a unitary relationship between Taxpayer and the 15 foreign subsidiaries at issue in this protest. However, after reviewing and considering both the case law and New Mexico statute addressing unitary businesses, the record demonstrates sufficient preponderant evidence that Taxpayer was unitary with 14 of the 15 foreign subsidiaries at issue in this protest.

a. General Overview of Corporate Income Tax Principals as they Relate to Unitariness.

Subject to the limitations of the United States Constitution's Due Process and Commerce Clause, under NMSA 1978, Section 7-2A-3, New Mexico levies an income tax on "the net income of every domestic corporation and upon the net income of every foreign corporation employed or engaged in the transaction of business in, into or from this state or deriving any income from any property or employment within this state." As used under the Corporate Income and Franchise Tax Act, the term "corporations" includes corporations, joint stock corporations, certain real estate trusts, financial corporations, banks, other business associations, limited liability companies, and partnerships taxed as corporations under the Internal Revenue Code. *See* NMSA 1978, § 7-2A-2 (D). Taxpayer is an out-of-state corporation engaged in transaction of business into and from New Mexico, subjecting Taxpayer to New Mexico's corporate income tax in the pertinent tax year.

Generally, states may not impose an income tax on the value earned outside of their borders under the Due Process and Commerce Clauses of the United States Constitution. *See ASARCO Inc. v. Idaho State Tax Commission*, 458 U.S. 307, 314 (1982). Specifically, the Commerce and Due Process Clauses of the United States Constitution impose distinct but parallel limitations on New Mexico's power to tax value earned from out-of-state business activities. *See Mobil Oil Corp. v. Comm'r of Taxes*, 445 U.S. 425, 454 (1980); *Norfolk & Western R. Co. v. Missouri Tax Comm'n.*, 390 U.S. 317, 325, n.5 (1969). A state may tax an apportioned share of a multistate entity's income earned outside of its territory if the activity that generated that income was part of a "unitary business." *MeadWestvaco Corp. v. Ill. Dep't of Revenue*, 553 U.S. 16, 19 (2008); *Allied-Signal, Inc. v. Dir., Div. of Taxation*, 504 U.S. 768, 772 (1992); *Hunt Wesson v. Franchise*

Tax Bd., 528 U.S. at 460; *Exxon Corp. v. Wisconsin*, 447 U.S. 207, 224 (1980); *Mobil Oil Corp.*, 454 U.S. at 442. "[T]he linchpin of apportionability in the field of state income taxation is the unitary-business principle." *Mobil Oil Corp.*, 445 U.S. 425, 439. However, a state may not tax a non-unitary, "nondomiciliary corporation's income… if it is derive[d] from unrelated business activity which constitutes a discrete business enterprise." *Allied-Signal, Inc,* 504 U.S. 768, 773 (internal citations omitted). Taxpayer bears the burden of establishing by clear and cogent evidence that the state seeks to tax extraterritorial values. *Allied-Signal, Inc.*, 504 U.S. 768, 782, citing *Exxon Corp*., 447 U.S. 207, 224.

b. Statutory Definition of Unitary Corporations.

Taxpayer's first argument challenging the unitariness of the foreign subsidiaries focuses on New Mexico's statutory definition of the term "unitary corporations." As applicable to tax year 2015, New Mexico statute defined "unitary corporations" as

> two or more integrated corporations, other than any foreign corporation incorporated in a foreign country and not engaged in trade or business in the United States during the taxable year, that are owned in the amount of more than fifty percent and controlled by the same person and for which at least one of the following conditions exists:
>
> (1) there is a unity of operations evidenced by central purchasing, advertising, accounting or other centralized services;
>
> (2) there is a centralized management or executive force and centralized system of operation; or
>
> (3) the operations of the corporations are dependent upon or contribute property or services to one another individually or as a group.

NMSA 1978, § 7-2A-2 (Q) (2014).

Taxpayer persuasively argues that since it owned less than a 5% stake in Oil Insurance Limited, that entity is not unitary with Taxpayer under the statutory definition. Because Taxpayer owned less than a 5% stake in Oil Insurance Limited rather than the 50% ownership requirement under the definition of Section 7-2A-2 (Q), Taxpayer was not unitary with Oil Insurance

Limited[7] under that statute. Consequently, the $18,588,489.00 in Oil Insurance Limited's generated dividends should be removed from Taxpayer's 2015 total foreign dividends.

Taxpayer argues that because the other 14 subsidiaries in dispute were foreign companies incorporated in a foreign country and did not engage in business in the United States during the tax year, those subsidiaries are excluded from the statutory definition of unitary corporations under the statutory clause reading "other than any foreign corporation incorporated in a foreign country and not engaged in trade or business in the United States during the taxable year." *Id.* This argument raises an issue of statutory construction.

Questions of statutory construction begin with the plain meaning rule. *See Wood v. State Educ. Ret. Bd.,* 2011-NMCA-20, ¶12. In *Wood*, ¶12 (internal quotations and citations omitted), the Court of Appeals stated "the guiding principle in statutory construction requires that we look to the wording of the statute and attempt to apply the plain meaning rule, recognizing that when a statute contains language which is clear and unambiguous, we must give effect to that language and refrain from further statutory interpretation." It is a canon of statutory construction in New Mexico to adhere to the plain wording of a statute except if there is ambiguity, error, an absurdity, or a conflict among statutory provisions. *See Regents of the Univ. of New Mexico v. New Mexico Fed'n of Teachers,* 1998-NMSC-20, ¶28, 125 N.M. 401. "Tax statutes, like any other statutes, are to be interpreted in accordance with the legislative intent and in a manner that will not render the statutes' application absurd, unreasonable, or unjust." *City of Eunice v. State Taxation & Revenue Dep't*, 2014-NMCA-085, ¶8 (internal citations and quotations omitted). If the plain language interpretation would lead to an absurd result not in accord with the legislative

[7] Moreover, there was very little in the evidentiary record about the role Taxpayer played in the operations, management, or control of Oil Insurance Limited, which also makes it difficult to determine whether the three unities existed between Taxpayer and Oil Insurance Limited, even beyond the ownership percentage statutory requirement.

intent and purpose it is necessary to look beyond the plain meaning of the statute. *See Bishop v. Evangelical Good Samaritan Soc'y*, 2009-NMSC-036, ¶11, 146 N.M. 473. Application of the plain meaning rule requires some caution because of its beguiling simplicity, particularly when there are potential contradictory statutory provisions at play. *See State ex rel. Helman*, 1994-NMSC-023, ¶23, 117 N.M. 346.

When applying the plain meaning rule, statutory sections should be read in harmony with each other, with statutes dealing with the same subject matter, and with the presumption that the Legislature was aware of relevant common law. *See State v. Trujillo*, 2009-NMSC-012, ¶22, 146 NM 14. *See also Hayes v. Hagemeier*, 1963-NMSC-095, ¶9, 75 N.M. 70 ("All legislation is to be construed in connection with the general body of law."). *See also N.M. Indus. Energy Consumers v. N.M. Pub. Regulation Comm'n*, 2007-NMSC-053, ¶ 20, 142 N.M. 533 (Legislature presumed to have knowledge of relevant statutes and the common law and thus statutes must be read in harmony with other statutes *in pari materia*). As the Court of Appeals recently reiterated,

> [i]n construing a statute, we observe the general principles that the plain language of a statute is the primary indicator of legislative intent and that when several sections of a statute are involved, they must be read together so that all parts are given effect.

Helmerich Payne Int'l Drilling Co. v. N.M. Taxation & Revenue Dep't, 2019-NMCA-054, ¶4, (internal citations omitted).

Taxpayer's narrow statutory reading of the conditional clause of Section 7-2A-2 (Q) excluding foreign corporations not otherwise engaged in United States business from the unitariness consideration is not compelling. Reviewing the complete statutory definition in harmony, as the case law requires, leads to the conclusion that the Legislature's purpose in codifying the definition of "unitary corporations" into statute was to adopt the well-understood, three unities test developed by case law. The three numbered subparts of Section 7-2A-2 (Q) constitute in sum and substance the three conditions under the common law's three unities test, as articulated in Supreme Court jurisprudence on unitary businesses for some 50-years. Indeed, by adopting the sum and substance of the three unities test, the Legislature was clearly attempting to adopt the common law understanding of a unitary corporation into the statutory definition under Section 7-2A-2 (Q). *See N.M. Indus. Energy Consumers*, 2007-NMSC-053, ¶ 20.

By reading the statutory definition holistically, if the activities of the foreign subsidiary satisfy the three numbered subparts of Section 7-2A-2 (Q), that foreign subsidiary would have substantially contributed to the flow of value to the domestic corporation engaged in business and trade in New Mexico. A foreign corporation's contribution of value, as demonstrated by meeting the three subparts of the statute, to the domestic entity engaged in New Mexico business activity would necessarily mean it had engaged in activity in the United States through its unitary relationship with the domestic corporation. This holistic reading of all terms of the statute together is much more in line with the Legislative intent and structure of the unitary corporation definition than Taxpayer's narrower, literal reading of just one portion of that section. *See Helman*, 1994-NMSC-023, ¶23, 117 N.M. 346 (the plain meaning rule requires some caution because of its beguiling simplicity, particularly when there are potential contradictory statutory provisions).

c. The Three Hallmark Elements of a Unitary Business.

While states cannot impose an income tax on the value earned outside of its border under the Due Process and Commerce Clauses of the United States Constitution, states are permitted to tax unitary activities occurring outside of their borders when those unitary activities contribute to the operation of a company's overall business as a whole. *See F.W. Woolworth Co. v. Taxation and Revenue Dep't*, 458 U.S. 354, 363–64, (1982). Separate corporate divisions that nevertheless benefit from functional integration, centralization of management, and economies of scale as part of a highly integrated line of business constitute unitary business regardless of the separate corporate and accounting structure employed. *See Exxon Corp.*, 447 U.S. 207, 224-226 (1980).

The United States Supreme Court has held over the years in a wide range of factual contexts that the constitutional test for establishing whether two or more companies are unitary is dependent on whether there is functional integration, centralization of management, and economies of scale between the companies. *See F.W. Woolworth Co.,* 458 U.S. 354; *See also ASARCO*, 458 U.S. 307 (1982); *See also Exxon Corp.*, 447 U.S. 207 (1980). These three elements indicate a flow of value between the subsidiary and the parent entity that passes constitutional muster as a unitary business subject to state taxation. *See Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159, 178–79 (1983). Indeed, these three elements—functional integration, centralization of management, and economies of scale—have become the "hallmarks" of a unitary relationship. *MeadWestvaco Corp.*, 128 S. Ct. 1498, 1508 (internal citations removed). Colloquially, functional integration, centralization of management, and economies of scale also constitute the three unities test of determining whether the businesses are unitary.

Additionally, the Supreme Court stated in *Allied-Signal, Inc.* that a non-domiciliary state can tax income from intangible property even if the income payer and payee are not engaged in the same unitary business, so long as the capital transaction serves an operational function, and not an investment function. *See Allied-Signal, Inc.*, 504 U.S. at 787. Hence, for example, a state may include in the apportionable income of a non-domiciliary corporation interest earned on short-term deposits in a bank located in another state if the deposits form part of the working capital of the corporation's unitary business. *Id*. In *Container Corp.*, the Supreme Court also noted that capital transactions can serve an investment function or an operational function, finding that corn futures contracts in the hands of a corn refiner seeking to hedge against increases in corn prices are operational rather than capital assets. *Container Corp.*, 463 U.S. 159, n.19; citing *Corn Products Refining Co. v. Commissioner*, 350 U.S. 46, 50-53 (1955).

In its 2008 decision in *MeadWestvaco Corp.*, the Supreme Court clarified its statement in *Allied-Signal, Inc.* In *MeadWestVaco*, the Court noted that its references to operational function in *Container Corp*. and *Allied-Signal, Inc.* were not intended to modify the unitary business principle by adding a new ground for apportionment. The Court explained that the concept of operational function simply recognized that an asset can be part of a taxpayer's unitary business even if the unitary business relationship doesn't exist between the payee and the payor. In the example given by the Court in *Allied-Signal, Inc.*, the taxpayer was not unitary with its banker, but the taxpayer's short-term deposits (which represented working capital and thus operational assets) were clearly unitary with the taxpayer's business. In *Corn Products*, the taxpayer was not unitary with the counterparty to its hedge, but the taxpayer's futures contracts (which served to hedge against the risk of an increase in the price of a key cost input) were likewise clearly unitary with the taxpayer's business. In the examples in *Allied-Signal, Inc.* and *Corn Products*, the payor was not a part of the taxpayer's unitary business but the asset clearly was. The conclusion that the asset served an operational function was merely instrumental to the constitutionally relevant conclusion that the asset was a part of the unitary business being conducted in the taxing state rather than a discrete asset to which the state had no claim.

Distilling the Supreme Court's constitutional jurisprudence in this area into a brief summary, pursuant to the holdings in *Allied-Signal, Inc.* and *MeadWestVaco*, an item of income is subject to apportionment if either (1) the taxpayer/payee and the income payor are engaged in a unitary business under the three unities test, or (2) the asset that generated the income was itself used as part of the taxpayer's unitary business operations in the taxing state[8].

d. Under the Three Unities Test, Taxpayer is Unitary with the remaining 14 subsidiaries.

In this case, Taxpayer carries the burden under the constitutional analysis to show by clear and cogent evidence that the state seeks to tax extraterritorial values. *Allied-Signal, Inc.*, 504 U.S. 768, 782, citing *Exxon Corp*., 447 U.S. 207, 224. Taxpayer is unable to meet that burden because application of the three unities test shows Taxpayer was unitary with the fourteen subsidiaries.

As to the centrally managed assets portion of the three unities test, the preponderance of evidence established centralized management between Taxpayer and the fourteen remaining foreign subsidiaries. The evidence established that Taxpayer and the fourteen remaining foreign subsidiaries were in the same line of business, oil and gas exploration and production. Taxpayer wholly owned all the fourteen remaining foreign subsidiaries. Taxpayer funded the acquisition of the subsidiaries, either through direct loans or investment of Taxpayer assets. Taxpayer shared common officers with the subsidiaries. All the fourteen remaining foreign subsidiaries shared a common management structure and system with Taxpayer. Taxpayer set target rates of return for these subsidiaries. Taxpayer approved all the subsidiaries' budgets, approved all capital expenditures over $10,000,000.00, and approved mergers and acquisitions by the subsidiaries. Taxpayer made the decision to defer income from the subsidiaries, when to reinvest the subsidiary income abroad, or when to distribute the income in the form of dividends, all of which show that Taxpayer is the one who exercised meaningful control over the important management functions of the subsidiaries. Taxpayer treated all its operations as one segment of

[8] It is possible that the unitary asset rationale of *Allied-Signal.*, *MeadWestVaco*, and *Corn Products* might extend to Oil Insurance Limited. However, the evidentiary record was inadequately developed to make such a determination.

business, according to its various 10K S.E.C. filings. Taxpayer made the decision to divest of the subsidiaries for the purpose to help pay down Taxpayer's debt and repurchase Taxpayer stock.

Taxpayer argues that there was insufficient evidence that New Mexico in any way contributed to the foreign subsidiary dividend generation either in the period of accumulation or in 2015. However, this argument is not persuasive. Taxpayer began acquiring the foreign subsidiaries in 1993. By 1993, the Permian Basin was one of Taxpayer's main oil production regions in North America, making Taxpayer's success as a unitary oil and gas production company at least partially dependent on Taxpayer's New Mexico activities in the Permian Basin. Permian Basin oil provided a major portion of Taxpayer's business product, the sale of which generated to Taxpayer a portion of the income it used in 1993 and beyond to acquire, invest, and grow the foreign subsidiaries. This establishes a connection between Taxpayer's New Mexico business activities and the acquisition, development, and growth of the foreign subsidiaries.

The importance of Taxpayer's operations in the Permian Basin as part of Taxpayer's unitary business success only grew further towards and into 2015. As Taxpayer pursued it strategic rebalancing, where it hoped to recalibrate its resources towards the North American market, Taxpayer repeatedly emphasized its focus and growth in the Permian Basin. The connection between New Mexico and the foreign subsidiaries is that the Permian Basin helped provide the product that fueled Taxpayer's unitary business and part of the income that Taxpayer invested into the foreign subsidiaries initially, to allow Taxpayer to leave the foreign income to grow over an extended period, and then subsequently to allow Taxpayer to maximize its return on investment from those foreign subsidiaries. Taxpayer used that return on investment to further Taxpayer's footprint in the more stable North American market, including additional growth in the Permian Basin in 2015. This is strong evidence that Taxpayer exercised central asset management to further its unitary oil and gas production business, and that assets related to Taxpayer's New Mexico operations both before (when the dividends were accumulating) and during 2015 played an important role in that asset management.

The preponderance of evidence established functional integration between Taxpayer and the fourteen remaining foreign subsidiaries under the second portion of the three unities test. Taxpayer and the fourteen remaining foreign subsidiaries shared numerous important corporate functions: legal operations, accounting operations, common set of accounts for purposes of S.E.C. reporting, internal audit functions, common HR policies and standards for employees, and common insurance. The fourteen remaining foreign subsidiaries used Taxpayer's logo. Taxpayer had access to the subsidiaries' IT software from Taxpayer's headquarters. The fourteen remaining foreign subsidiaries utilized Taxpayer's performance measures tracking system. Taxpayer used foreign subsidiary earnings to acquire other foreign assets and subsidiaries in its line of business. As discussed in the previous paragraph, Taxpayer used the dividends to help fuel expansion of its North American operations in 2015, including growth in the Permian Basin.

While the evidence of centralized management and functional integration are fairly strong, the three unities factor of economies of scale between Taxpayer and the fourteen remaining foreign subsidiaries is a much closer analysis and largely just a reiteration of the functional integration and centralized management factors. Nevertheless, the evidence is still sufficient to find by the preponderance that Taxpayer and its subsidiaries benefitted from economies of scale. Taxpayer and its subsidiaries were in the same line of business: oil and gas exploration, production, and sales. Taxpayer invested in these subsidiaries (including in 2015, as shown by the Schedule F of Form 5471) to increase its production and sales of oil and gas, and the subsidiaries used Taxpayer's mode of operations—not only in the sense of Taxpayer's theoretical corporate attitude but also practical shared structures like corporate accounting, audits, legal, HR policies, budgeting, and shared corporate officers—in an effort to maximize production and sales of oil and gas while minimizing administrative costs and burdens. "When a corporation invests in a subsidiary that engages in the same line of work as itself, it becomes much more likely that one function of the investment is to make better use—either through economies of scale or through operational integration or sharing of expertise—of the parent's existing business-related resources. *Container Corp.,* 463 U.S. 159, 178.

Taxpayer criticizes the Department's evidence on the issue of unitariness between Taxpayer and its subsidiaries. Taxpayer argues that the Department did not present evidence specific to tax year 2015, reached strained conclusions and assumptions from the limited evidence it presented, and failed to produce any evidence about eight of Taxpayer's subsidiaries. The hearing officer disagrees. The Department presented the subsidiary business connection questionnaires from five of the fifteen subsidiaries. Mr. Sauer confirmed that Taxpayer's answers on the five subsidiaries business connection questionnaires, and in turn his answers during his testimony about those same five subsidiaries, applied in a substantially similar manner to the remaining nine foreign subsidiaries. The Department presented Taxpayer's 10K Form for nearly a decade before 2015, where Taxpayer asserted it operated as one line of business. Additionally, while Taxpayer argued that the foreign subsidiaries were largely self-funding, the record contained evidence showing that many of the foreign subsidiaries benefitted from significant Taxpayer investments in 2015, as indicated in the various Form 5471 Schedule F's and supporting documentation.

Protest Auditor Mary Griego competently, credibly, and persuasively testified about her review of the business questionnaires, the 10Ks, and the Apache 40 at 40 history of the company, weaving those items and the testimony at hearing together to show the unitary relationship between Taxpayer and its subsidiaries. To the extent that Taxpayer argues that the burden shifted to the Department to reestablish the correctness of its assessment vis-à-vis unitariness (an argument that the hearing officer does not find compelling considering the narrow ruling on the presumption of correctness issue addressed above), Ms. Griego's credible and persuasive testimony was sufficient to reestablish the presumption of correctness on that issue. Additionally, Ms. Griego articulated the Department's efforts to obtain additional information about Taxpayer's relationship with its subsidiaries at acquisition and through tax year 2015, efforts in which Taxpayer, for various reasons, declined to participate. In sum, despite Taxpayer's attacks, under the preponderance standard, there is sufficient evidence to support a unitary relationship between Taxpayer and the fourteen remaining foreign subsidiaries at issue.

Regardless of Taxpayer's complaints about the Department's evidence of unitariness, Taxpayer failed to carry its own burden of persuasion showing that the state was attempting to tax non-unitary, extraterritorial income. *See Allied-Signal, Inc.*, 504 U.S. 768, 782. Although perhaps employing a more sophisticated and evolved corporate structure, Taxpayer's fundamental business of maximizing oil and gas production and sales while minimizing administrative costs and burdens for Taxpayer and its subsidiaries is not remarkably different from the integrated oil and gas production businesses of Mobil Oil Corp. or Exxon Corp. in those landmark United States Supreme Court decisions. *See Mobil Oil Corp.*, 445 U.S. 425, 435 (although the record was minimal on the activities of the dividend-producing subsidiaries, it was nevertheless apparent from perusal of corporate reports that the entities were engaged in that taxpayer's integrated petroleum enterprise and that taxpayer failed to show that they entities did not contribute to that taxpayer's worldwide petroleum enterprise); *see also Exxon Corp*., 447 U.S. 207, 224, (efforts of the taxpayer to treat different entities as discrete business enterprises were insufficient for the taxpayer to carry its burden because the taxpayer was engaged in a highly integrated business that benefitted from centralized management and controlled interaction.).

The record evidence makes clear that Taxpayer benefitted with real flow of value to and from its subsidiaries. *See Container Corp*. Taxpayer actively invested money into the foreign subsidiaries dating back to 1991 and through the relevant time in 2015, a period when Taxpayer's unitary business success depended in part on Taxpayer's New Mexico operations in the Permian Basin. Taxpayer used the income from the dividends and dissolution of the subsidiaries to invest more resources back into its North American operations, including expanding Taxpayer's Permian Basin operations in 2015. As the New Mexico Court of Appeals has stated, "[t]he general premise underlying unitary taxation is that the value of a corporation's unitary business is apportionable to a state for taxation if the corporation's operations within the state contribute to the profitability of the entity's overall business." *NCR Corp. v. Taxation & Revenue Dept.*, 1993-NMCA-060, ¶ 15, 115 N.M. 612, 616. There can be little doubt that Taxpayer's holdings in the Permian Basin contributed to Taxpayer's overall enterprise of oil and gas production across the globe. In turn, New Mexico may tax an apportioned share of Taxpayer's unitary business income.

Issue Three: The Dividends, Subpart F, and Check-the-box Income Constitute Business Income.

Taxpayer argues that its foreign-source dividend income, its Subpart F income, and its check-the-box deemed income is not business income subject to apportionment in New Mexico but is non-business income subject to allocation to Taxpayer's domiciliary state of Texas. To the contrary, the Department argues that all such income is business income subject to fair apportionment in New Mexico. The Department's argument is persuasive, as the foreign-source dividend income, Subpart F income, and the check-the-box deemed income all qualify as business income under applicable New Mexico authority.

UDITPA distinguishes between business income and nonbusiness income: only business income is subject to apportionment for purposes of state income tax imposition. *See* NMSA 1978, §7-4-10 (A) (2013) ("…all business income shall be apportioned..."). Rather than apportioned to multiple states for imposition of commensurate share of income taxes, nonbusiness income is allocated only to the taxpayer's domiciliary state and only that state may impose an income tax on the nonbusiness income. "Business income" is defined under NMSA 1978, Section 7-4-2 (A) (1999), as

> …income arising from transactions and activity in the regular course of the taxpayer's trade or business and income from the disposition or liquidation of a business or segment of a business. "Business income" includes income from tangible and intangible property if the acquisition, management or disposition of the property constitute integral parts of the taxpayer's regular trade or business operations.

In contrast, "nonbusiness income" is defined under UDITPA as "all income other than business income." NMSA, §7-4-2 (E).

Numerous Department regulations provide further guidance on the UDITPA distinction between business and nonbusiness income. In addition to essentially reiterating the statutory definition of business income, Department Regulation 3.5.1.9 (A) NMAC adds that "[i]n essence, all income which arises from the conduct or the disposition or liquidation of trade or business operations of a taxpayer is business income." Regardless of the name, label, or classification used to describe the income, Department Regulation 3.5.1.9 (A) NMAC indicates that

> [i]ncome of any type or class and from any source is business income if it arises from transactions and activity occurring in the regular course of a trade or business. Accordingly, the critical element in determining whether income is "business income" or "nonbusiness income" is the identification of the transactions and activity which are the elements of particular trade or business. In general, all transactions and activities of the taxpayer which are dependent upon or contribute to the operations of the taxpayer's economic enterprise as a whole constitute the taxpayer's trade or business and will be transactions and activity arising in the regular course of, and constitute integral parts of, a trade or business.

Conceptually, New Mexico's statutory scheme under Section 7-4-2 (A) adopts three tests to determine whether the income is business or non-business income. First, under Section 7-4-2 (A), is a "transactional test," where income is considered business income when the income arose from "transactions and activity" occurring in the "regular course of the taxpayer's trade or business."

The second test under Section 7-4-2 (A) is called the "disposition test." Under the disposition test, income is considered business income when the income arose from the disposition of a business or segment of a business. *See* § 7-4-2 (A). This dispositional test portion of the statute was added by the Legislature in response to the New Mexico Court of Appeals' decision in *McVean & Barlow, Inc. v. Bureau of Revenue*, 1975-NMCA-128, 88 NM 521. In *McVean & Barlow, Inc.*, the Court of Appeals found that income from the liquidation of a line of business was non-apportionable, non-business income under UDITPA because it arose from a one-time transaction not part of that taxpayer's line of business. This statutory overruling of *McVean & Barlow, Inc.* made clear that the Legislature intended the proceeds from the disposition of a line of business to be considered business income under UDITPA subject to apportionment, whether or not the disposition was a one-time transaction.

The third test, found under Section 7-4-2 (A)'s last sentence, is the "functional test." Under the functional test, income is considered business income when the income arose from "tangible and intangible property if the acquisition, management or disposition of the property constitute an integral part of the taxpayer's regular trade or business operations."

As the Department persuasively argues, Taxpayer's foreign dividend income and Subpart F income amounted to business income subject to New Mexico apportionment under Section 7-4-2 (A)'s dispositional and functional tests. Much of Taxpayer's counter-argument assumes that there is a non-unitary relationship between Taxpayer and the subsidiaries. Without repeating the unitary analysis of the previous section, Taxpayer was unitary with all but one of the foreign subsidiaries that produced the income in question in 2015. As such, the subsidiaries' dividend income and Subpart F income, which Taxpayer used to bolster its North American operations including in the Permian Basin, contributed to Taxpayer's economic enterprise and trade or business, satisfying Regulation 3.5.1.9 (A) NMAC's standard for business income. Even though Subpart F income constitutes unrealized, deemed income, it is nevertheless subject to New Mexico apportionment. *See NCR Corp.*, 1993-NMCA-060, ¶¶ 26-34 (New Mexico Court of Appeals held that the Subpart F income of unitary foreign-source dividend income is business income subject to New Mexico apportionment).

Even under Taxpayer's theory of the one-time disposal of some of the foreign subsidiaries, Taxpayer undertook the one-time strategic rebalancing of its global operations to refocus on North American operations. As part of this process, Taxpayer sold off some assets (or all in the case of the Australian and Argentinian subsidiaries) of the foreign subsidiaries at issue for the express purpose of paying off Taxpayer debt, purchasing back Taxpayer stock, and expanding Taxpayer's North American operations. Taxpayer used its foreign assets to bolster its North American line of business with its more predictable rates of return. During this time, Taxpayer grew its Permian Basin holdings, which helped power its North American growth.

In its Form 10k's filed during the years of the rebalancing, Taxpayer reported that its strategic rebalancing was highly successful, resulting in the sale of $7,000,000,000.00 in assets, reduction of debt by $2,600,000,000.00, and the repurchasing over $1,000,000,000.00 in stock. Taxpayer used this income to focus and expand its core operations in North America (including in New Mexico's Permian Basin), reduce its debts, and buy back its stock, all activities that are integral to Taxpayer's core business operations. These facts satisfy both the dispositional and functional tests for business income.

Whether or not this was a one-time undertaking has little bearing in the analysis after the Legislature overruled *McVean & Barlow, Inc.* As Mr. Sauer acknowledged, the purpose of disposing of these assets was to further Taxpayer's core North American business. In so disposing of the assets in a manner integral to Taxpayer's business, the dividend and Subpart F income was business income under Section 7-4-2.

Taxpayer argues that the check-the-box election deemed income is non-business income because it is purely fictional income not involving a real transaction or activity for the purposes of the definition of business income. Under Form 8832, a check-the-box election caused two of Taxpayer's foreign subsidiaries to be reclassified on paper from associations to disregarded entities. This check-the-box election fictional disposition occurred pursuant to 26 C.F.R.§301.7701-3(g)(1)(iii). Under 26 C.F.R. § 301.7701-3, "[i]f an eligible entity classified as an association elects… to be disregarded as an entity separate from its owner, the following is deemed to occur: The association distributes all of its assets and liabilities to its single owner in liquidation of the association."

While Taxpayer realized no actual income from the check-the-box election through a real transaction, sale, or disposition, 26 C.F.R. § 301.7701-3 still required Taxpayer to include the deemed liquidation income as federal income under its federal return. New Mexico, in turn, captured the inclusion of this deemed income on Taxpayer's federal return as part of Taxpayer's New Mexico corporate income tax base income. *See* NMSA 1978, § 7-2A-2 (C) (2017) (defining New Mexico corporate "base income" as federal taxable income as calculated under the Internal Revenue Code.).

In *NCR Corp.*, a taxpayer argued that the Subpart F income was hypothetical income not taxable until actually realized and distributed. *NCR Corp.*, 1993-NMCA-060, ¶28 & 30. That argument is remarkably similar to Taxpayer's argument in this protest, that the check-the-box election resulted in a hypothetical versus actual distribution of income. The Court of Appeals rejected that approach with respect to the similar deemed Subpart F income, finding in part that if the federal government required inclusion of the deemed income it was appropriate for New Mexico to apportion the deemed income as unitary business income. *See id.* at ¶31-34. The logic of the Court of Appeals' conclusion in *NCR Corp.* extends to the deemed, hypothetical check-the-box income required to be included under 26 C.F.R. § 301.7701-3 and captured as New Mexico base income under Section 7-2A-2 (C).

While Taxpayer did cite to three out-of-state cases discussing the check-the-box election deemed income where the taxpayers prevailed, none of those cases stand for the broad proposition that hypothetical, unrealized, deemed income cannot constitute business income. *See Manpower, Inc. v. Comm'r of Revenue*, 724 N.W.2d 526 (Minn. 2006) (check-the-box election does not alter an entity's status as foreign or domestic); *see also Ashland Inc. v. Comm'r of Revenue*, 899 N.W.2d 812 (Minn. 2017) (Minnesota required to recognize check-the-box election income as part of state's net income determination); *see also Deere & Company, Petitioner v. Wisconsin Department of Revenue, Department*, 2019 WL 4308827 (Wisconsin tax court found that check-the-box election income qualifies for state dividends received deduction). In fact, there seemed to be little dispute in those cases that the hypothetical, deemed income could theoretically constitute business income if otherwise permitted under state tax law. Instead, the outcome of those cases turned on the corollary consequences of the check-the-box election in other state-specific areas of tax law. In any event, *NCR Corp*. makes clear that hypothetical, deemed income can constitute business income in New Mexico if the federal tax code requires inclusion of such deemed income. *See NCR Corp*. at ¶31-34.

This permissible inclusion and treatment of the hypothetical, deemed income is also consistent with Department Regulation 3.5.1.9 (A) NMAC's definition that "[i]ncome of *any type* or class and from *any source*…" (emphasis added) can be considered business income. Because the federal regulation requires the deemed distribution and liquidation of the assets, the income meets the "any type" or "any source" language of that regulation. Since the deemed income check-the-box otherwise came from the unitary foreign subsidiaries, the income also satisfied the dispositional and functional business income test. As such, Taxpayer's check-the-box election income is business income, subject to state apportionment.

Issue Four: Taxpayer's Foreign Commerce Discrimination Claim Fails

Taxpayer argues in this case that the Department's assessment violates the Foreign Commerce Clause of the constitution under the holding of *Kraft Gen. Foods v. Iowa Dep't of Revenue & Fin.*, 505 U.S. 71 (1992), with its disparate treatment of foreign subsidiary income depending on the corporate income tax filing method used. The Department contends that there is no foreign commerce violation in taxing an apportioned share of the unitary income of a combined return filer, citing numerous cases that will be discussed in more detail as part of the resolution of this issue. This is a complex issue that requires a contextual discussion of corporate income tax reporting methods and structures, as well as detailed review of case law history and developments from multiple jurisdictions.

New Mexico's corporate income tax structure allows a taxpayer subject to the Corporate Income and Franchise Tax Act to elect one of three reporting methods. *See* Regulation 3.4.10.8 (B) NMAC. The first permissible reporting method is the separate corporate entity method. *See* Regulation 3.4.10.8 (B) (1) NMAC and Regulation 3.4.10.7 (A) NMAC. This method entails allowing each corporation doing business in New Mexico, even if it is part of a larger unitary group, to file a separate corporate income tax in New Mexico. As will be discussed in much greater detail, the New Mexico Supreme Court has expressly prohibited the state from including foreign dividend income for separate method filers because under the structure of the taxing scheme, domestic dividends were provided favorable treatment over foreign dividends in contradiction to the Foreign Commerce Clause. *See Conoco, Inc. v. New Mexico Taxation and Revenue Department*, 1997-NMSC-005, 122 N.M. 736 (1996). In recognition of the clear *Conoco, Inc.* holding, Department Regulation 3.4.1.12 NMAC (1998) now allows a separate entity corporate filer to exclude foreign source dividends from its base income.

The second permissible reporting method is the combination of unitary corporations, also commonly referred to as a combined return or as combined reporting. *See* NMSA 1978, § 7-2A-8.3 (2013) and Regulation 3.4.10.8 (B) (2) NMAC. This is the reporting method Taxpayer used in this protest. Generally, this method requires a corporation to report the combined income of all its unitary subsidiaries on one return. In their preeminent State Taxation treatise, Hellerstein and

Hellerstein note that "[t]he purpose of the combined reporting is to determine the income or other tax base of the in-state taxpayer by viewing the taxpayer as part of the unitary business, and applying the apportionment factors of the entire unitary business to the taxable net income of the unitary business." *See J. Hellerstein & W. Hellerstein*, ¶8.11[1]. The New Mexico Court of Appeals upheld New Mexico's combined return reporting treatment against a Foreign Commerce Clause challenge. *See NCR Corp.*, 1993-NMCA-060. Additionally, in a previous administrative decision discussed in more detail below, the combined return reporting method treatment of dividends was found to not offend the Foreign Commerce Clause. *See In the Matter of the Protest of Xerox Corporation*, Taxation and Revenue Decision and Order No. 03-22, Dec. 3, 2003, 2003 WL 24889474, (non-precedential; publicly available at http://realfile.tax.newmexico.gov/03-22__xerox_corporation.pdf) (referred to as "*Xerox*").

The third reporting method is the federal consolidated group. *See* NMSA 1978, § 7-2A-8.4 (1993) and Regulation 3.4.10.8 (B) (3) NMAC. Under Section 7-2A-8.4,

> [a]ny corporation that is subject to taxation under the Corporate Income and Franchise Tax Act [7-2A-1 NMSA 1978] and that reports to the internal revenue service for federal income tax purposes its net income consolidated with the net income of one or more other corporations may elect to report to New Mexico on the same basis.

The New Mexico consolidated group reporting method is premised on the corporation reporting income federally on a consolidated group basis. Under the I.R.C., 26 U.S.C. § 1501 establishes the privilege of filing a federal consolidated return for an affiliated group of corporations, as defined by 26 U.S.C. § 1504. Under the definition contained in NMSA 1978, Section 7-2A-2 (A) (2014), New Mexico incorporates the I.R.C. definition of an affiliated group. An affiliated corporation is a corporation connected through stock ownership amounting to 80% of voting power or value with a common parent corporation. *See* 26 U.S.C. § 1504 (A). Foreign corporations may not be included in a consolidated group. *See* 26 U.S.C. § 1504 (B). Similar to the rationale from the earlier *Xerox* administrative decision, the undersigned hearing officer recently found the consolidated group reporting method treatment of dividends did not offend the Foreign Commerce Clause. *See In the Matter of the Protest of General Electric Company & Subsidiaries*, Administrative Hearings Office Decision and Order No. 18-12, April 6, 2018, 2018 WL 1795457, (non-precedential; publicly available at https://www.tax.newmexico.gov/all-nm-taxes/tax-decisions-orders/)(referred to as "*General Electric*").

On questions of whether there is a violation of the foreign commerce clause, there is a six-factor test. *See Japan Line, Ltd. v. Cty. of L.A.*, 441 U.S. 434, 451 (1979). The first four factors of the analysis are the traditional four Commerce Clause Factors articulated in *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977): (1) a sufficient nexus exists between the activity being taxed and the taxing state; (2) the tax is fairly apportioned; (3) the tax does not discriminate against interstate commerce; and (4) the tax is fairly related to services provided by the state. On questions related to the Foreign Commerce Clause, the United States Supreme Court has added two additional factors: (1) "whether the tax creates a substantial risk of international multiple taxation"; and (2) "whether the tax prevents the Federal Government from speaking with one voice when regulating commercial relations with foreign governments." *Japan Line*, 451.

In *Japan Line*, the United States Supreme Court held that California could not tax a foreign corporation engaged in shipping without violating the Foreign Commerce Clause because the tax in question would result in multiple taxation and because it was an impediment to the federal government's authority to speak with one voice on foreign trade. The United States Supreme Court was motivated to add the two additional Foreign Commerce Clause factors in *Japan Line* at 447-448 (internal citations omitted) because of the possibility of unaddressable multiple taxation:

> …neither this Court nor this Nation can ensure full apportionment when one of the taxing entities is a foreign sovereign. If an instrumentality of commerce is domiciled abroad, the country of domicile may have the right, consistently with the custom of nations, to impose a tax on its full value. If a State should seek to tax the same instrumentality on an apportioned basis, multiple taxation inevitably results. Hence, whereas the fact of apportionment in interstate commerce means that "multiple burdens logically cannot occur," the same conclusion, as to foreign commerce, logically cannot be drawn. Due to the absence of an authoritative tribunal capable of ensuring that the aggregation of taxes is computed on no more than one full value, a state tax, even though "fairly apportioned" to reflect an instrumentality's presence within the State, may subject foreign commerce "'to the risk of a double tax burden to which [domestic] commerce is not exposed, and which the commerce clause forbids.'"

Shortly after issuance of *Japan Line*, the United States Supreme Court again addressed questions of state taxation vis-à-vis foreign commerce. In *Mobil Oil Corp.*, 445 U.S. 425 (1980), the multinational Mobil Oil Corp., which conducted much of its business through wholly or partially owned domestic and foreign subsidiaries, had subtracted all its foreign dividends from its net income on its Vermont Corporate Income Tax Return. *See Mobil Oil Corp.*, 445 U.S. 425, 428-431. Taxpayer in this protest effectively did the same thing as Mobil Oil Corp., essentially removing its foreign dividend income from New Mexico net income on its original CIT-1 return. Like the Department in this protest, Vermont in *Mobil Oil Corp.* assessed Mobil Oil Corp. the tax attributable to Vermont's recalculation and inclusion of foreign dividends in the apportionable income tax base. *See id*. at 430-431. Mobil Oil Corp. contended that inclusion of this income violated the Due Process Clause, the Commerce Clause, and the Foreign Commerce Clause and that the inclusion of the foreign dividends would result in an unfair and inequitable apportionment of the income attributable to Vermont. *See id*. at 432.

As part of its various challenges, Mobil Oil Corp. also argued that, under *Japan Line*, the inclusion and apportionment of the foreign source dividend income would result in a substantial risk of impermissible multiple taxation. *See id*. at 442. As such, Mobil Oil Corp. contended that "because of the risk of multiple taxation abroad, allocation of foreign-source income to a single situs is required at home. Appellant's reasoning tracks the rationale of *Japan Line*, that is, that allocation is required because apportionment necessarily entails some inaccuracy and duplication." *Id*. 446.

The Supreme Court rejected Mobil Oil Corp.'s argument, distinguishing between the property taxes assessed in *Japan Line*, where situs was an important consideration, and an apportioned income tax, where situs is of far less importance. *See id*. at 445-446 and at 448. Ultimately, the Supreme Court held in *Mobil Oil Corp.* that nothing under the Due Process Clause or the Commerce Clause prevented Vermont from taxing its proportionate, apportioned share of Mobil Oil Corp. income, including the foreign-source dividend income. *See id*. at 449. This holding is instructive to the present protest given the similarity of Taxpayer's removal of the foreign source dividend income from its New Mexico return and New Mexico's effort to include that income in the fair apportionment of Taxpayer's New Mexico corporate income tax liability.

In 1983, four years after *Japan Line* and three years after *Mobil Oil Corp.*, the United States Supreme Court again discussed the application of the Foreign Commerce Clause to a state's attempt at taxation in *Container Corp.*, 463 U.S. 159 (1983). *Container Corp.* involved California's combined reporting taxation of a unitary series of entities. The Supreme Court analyzed three major issues in *Container Corp.*: first, whether that taxpayer and its foreign subsidiary were properly found to be a unitary business; second, whether the standard three-factor apportionment applied to a multinational business violated the constitutional requirement for fair apportionment; and third, whether the state had "an obligation under the Foreign Commerce Clause… to employ the 'arm's-length' analysis used by the Federal Government and most foreign nations in evaluating the tax consequences of intercorporate relationships?" *Container Corp.*, 463 U.S. at 163. The Supreme Court ultimately found, after a thorough and comprehensive analysis, that it was proper for the state to find a unitary business relationship under the facts of the case, proper for the state to apply the standard three-factor apportionment to taxpayer and its unitary subsidiaries, and that the Foreign Commerce Clause did not prohibit the tax or compel the state to employ the Federal Government's "arms-length" analysis. *See id.*at 184-197.

In analyzing the Foreign Commerce Clause component of the case in, *Container Corp.,* the Supreme Court clarified and distinguished a few key points from its previous ruling in *Japan Line*. First, the Supreme Court noted that *Japan Line* involved a property tax rather than an income tax at issue before it, which the court found minimized the importance of situs in the analysis. *Container Corp.*, 463 U.S. 159, 187-188. Second, the court noted that any potential double taxation, although a possibility, was not the result of California's formulary apportionment scheme. *Id.* Third, the Supreme Court noted that the tax in question was not directed at a foreign corporation, but instead fell on a domestic corporation doing business in the United States, a question it had expressly left unresolved in *Japan Line*. *Id*.

Because of these differences, the Supreme Court held in *Container Corp.* that imposition of taxation did not violate either of the two additional Foreign Commerce Clause factors articulated in *Japan Line*, the substantial risk of multiple taxation or interfering with federal government's ability to speak with one voice. *Container Corp.*, 463 U.S. at 187-196. In summary, the Supreme Court did not find in either *Container Corp.* or *Mobil Oil Corp.*, that a taxing scheme which taxed an apportioned shared of a unitary business with both foreign and domestic subsidiaries violated the Foreign Commerce Clause.

Unlike those two cases, in 1992 the United States Supreme Court did find a Foreign Commerce Clause violation in *Kraft,* 505 U.S. 71 (1992). The question at issue in *Kraft* was "whether the disparate treatment [by Iowa] of dividends from foreign and from domestic subsidiaries violates the Foreign Commerce Clause." *id*. at 73.

Similar to New Mexico's taxing scheme, Iowa's starting point for calculating corporate income tax was federal taxable income, which excludes domestic dividends from the income while leaving foreign dividends included in the taxable income. Again like New Mexico, and unlike the federal government, Iowa did not allow a subsequent credit for payment of foreign tax on foreign dividends, meaning that Iowa taxed a single filer corporation's foreign dividends but not its domestic dividends. *See id*. at 73-74. The Supreme Court held in *Kraft* that the disparate treatment inherent in Iowa's single-filer corporate tax scheme between foreign and domestic dividends amounted to facial discrimination against foreign commerce in violation of the Foreign Commerce Clause. *Id*.

Kraft did not specifically address combined returns, which is the type of return at issue in this protest. But in a much-cited footnote on the question of combined returns, the *Kraft* Supreme Court stated:

> If one were to compare the aggregate tax imposed by Iowa on a unitary business which included a subsidiary doing business throughout the United States (including Iowa) with the aggregate tax imposed by Iowa on a unitary business which included a foreign subsidiary doing business abroad, it would be difficult to say that Iowa discriminates against the business with the foreign subsidiary. Iowa would tax an apportioned share of the domestic subsidiary's entire earnings, but would tax only the amount of the foreign subsidiary's earnings paid as a dividend to the parent.

> In considering claims of discriminatory taxation under the Commerce Clause, however, it is necessary to compare the taxpayers who are "most similarly situated." A corporation with a subsidiary doing business in Iowa is not situated similarly to a corporation with a subsidiary doing business abroad. In the former case, the Iowa operations of the subsidiary provide an independent basis for taxation not present in the case of the foreign subsidiary. A more appropriate comparison is between corporations whose subsidiaries do not do business in Iowa.

Kraft, 505 U.S. 71, 80 n.23 (internal citations omitted).

In 1997, in *Conoco, Inc.*, 1997-NMSC-005, 122 N.M. 736, the New Mexico Supreme Court considered whether New Mexico's separate entity filer corporate income tax method, even with the Department's attempt at formulary apportionment factor relief pursuant to the Detroit Formula, survived Foreign Commerce Clause scrutiny in light of *Kraft*. The two taxpayers at issue in *Conoco, Inc.* had elected to file their respective New Mexico corporate income tax returns under the separate entity method. *Id*. at ¶6. Under that method, like in *Kraft*, the New Mexico Supreme Court noted that New Mexico's reliance on the federal taxable income resulted in the inclusion of foreign dividend income while excluding domestic dividend income from New Mexico corporate income tax. *Id*. at ¶7. Unlike the federal government, which the court noted has a subsequent credit for taxes paid to foreign governments designed to mitigate against the possibility of multiple taxation on foreign subsidiaries, New Mexico does not have a similar credit for foreign taxes paid after determination of federal base income, leading to those taxpayers' claim that New Mexico's statute, like Iowa's statute, facially discriminated against foreign commerce. *Id*.

The New Mexico Supreme Court carefully reviewed the *Kraft* decision, highlighting a few key parts of that decision that informed its analysis of the issue. The Court noted that Iowa and New Mexico used the same starting point, the federal taxable income as the base income, but that unlike Iowa, New Mexico used the Detroit Formula. *Id*. at ¶8. The New Mexico Supreme

Court noted that the United States Supreme Court had considered and rejected Iowa's argument that the offending provision was mitigated by the fact that a taxpayer could change their corporate structure or domicile to avoid the disparate treatment of dividends. *Id*. The New Mexico Supreme Court also cited the United States Supreme Court's rejection of Iowa's argument that the administrative efficiency in relying on the federal base income definition justified the statutory scheme. *Id.* at ¶9.

After reviewing the *Kraft* decision in more detail, the New Mexico Supreme Court then turned to a series of decisions from other states that considered the application of *Kraft* to their respective state tax obligations. The Court reviewed the Rhode Island decision, *Dart Industries, Inc. v. Clark*, 657 A.2d 1066 (R.I. 1995), where the Rhode Island Supreme Court had found that *Kraft* controlled the outcome in finding Rhode Island's tax scheme, similar to both Iowa and New Mexico, unconstitutional. *See Conoco, Inc.*, 1997-NMSC-005, ¶10. In particular, the New Mexico Supreme Court cited a portion of the *Dart Industries* decision where the Rhode Island Supreme Court had pointed out that "[a]lthough the Rhode Island and Iowa statutes differ in minor respects, the fatal flaw in the Iowa statute is present in the Rhode Island statute: a preference for domestic commerce over foreign commerce." *Id.* (citing *Dart Industries* at 1066).

The New Mexico Supreme Court then analyzed two state cases that reached an opposite conclusion from *Dart Industries* and *Kraft: In re Appeal of Morton Thiokol, Inc.*, 254 Kan. 23, 864 P.2d 1175 (Kan. 1993) and *E.I. Du Pont de Nemours & Co. v. State Tax Assessor*, 675 A.2d 82, (Me. 1996). *See Conoco, Inc.*, 1997-NMSC-005, ¶11-13. In *Morton Thiokol, Inc.*, the Kansas Supreme Court considered in pertinent part whether Kansas' combination method corporate filing scheme violated the Foreign Commerce Clause like Iowa's single filer scheme, as found in *Kraft*. *See Morton Thiokol, Inc.*, 254 Kan. 23, 864 P.2d 1175 (1993). The Kansas

Supreme Court noted that like Iowa, the Kansas tax base is determined by looking to federal taxable income. *See Morton Thiokol, Inc.*, 254 Kan. 23, 25, 864 P.2d 1175 (1993). The Kansas Supreme Court relied on footnote 23 from the *Kraft* decision in its analysis, finding that under that footnote, courts must be careful to select the appropriate comparison between similar circumstances. *See id*. at 36-37. The Kansas Supreme Court found that the taxpayer in that case was asserting an incorrect comparison of two non-combined subsidiaries that would not be subject to Kansas tax. *See id*. at 38.

In an extended passage quoted by the New Mexico Supreme Court in *Conoco, Inc.*, 1997-NMSC-005, ¶11, the Kansas Supreme Court stated:

> [In *Kraft*, t]he Supreme Court compared a parent corporation with a domestic subsidiary which does not do business in Iowa to a parent corporation with a foreign subsidiary which does not do business in Iowa. In this comparison, Iowa discriminated against the parent corporation with the foreign subsidiary because Iowa allowed a deduction for the dividends received by the parent with the domestic subsidiary, but not for the dividends received by the parent with the foreign subsidiary. . . [However,] *Kraft* "does not address the taxation of foreign dividends by domestic combination states." Clearly, *Kraft* does not hold that the taxation of foreign dividends by a combination method is facially unconstitutional. . . Allowing a deduction for the domestic dividend avoids double taxation. It is the use of the domestic combination method which distinguishes the Kansas and Iowa tax schemes.

Morton Thiokol, Inc., 254 Kan. at 37–38.

In light of that analysis, the Kansas Supreme Court resolved the pertinent issue before it by concluding that "[i]n a combined filing state, such as Kansas, the hypothetical parent's tax base includes the combined federal taxable income of its combined domestic subsidiaries as well as dividends from foreign subsidiaries. We conclude there is no showing that this method is discriminatory under the holding in *Kraft*; therefore, it is not violative of the federal Constitution's Commerce Clause (Art. I, § 8, cl. 3)." *Id*.

Another case that the New Mexico Supreme Court considered in *Conoco, Inc.*, was the Maine Supreme Judicial Court's decision in *Du Pont*. In that case, the Maine Supreme Judicial Court reached a similar conclusion to the Kansas Supreme Court about the applicability of *Kraft* to a combined filing state: Maine's water's edge combined reporting method provided a "taxing symmetry" between foreign and domestic dividends not present in Iowa's single filer method, making Maine's scheme distinguishable from the scheme rejected in *Kraft*. *See Du Pont*, 675 A.2d 82, 88. As the Maine Supreme Judicial Court expands,

> [f]ar from discriminating against foreign commerce, Maine's water's edge combined reporting method provides a type of "taxing symmetry" that is not present under the single entity system. **Although the dividends paid to parent corporations with domestic subsidiaries are not taxed, the apportioned income of the domestic subsidiaries is subject to tax. Because the income of the unitary domestic affiliates is included, apportioned, and ultimately directly taxed by Maine as part of the parent company's income, the inclusion of dividends paid by foreign subsidiaries does not constitute the kind of facial discrimination against foreign commerce** that caused the Supreme Court to invalidate Iowa's tax scheme in *Kraft*. Thus, Maine's use of a water's edge combined reporting method distinguishes Maine's taxing scheme from the scheme invalidated by the United States Supreme Court in *Kraft*.

Id. (emphasis added).

After reviewing *Kraft*, *Dart Industries, Morton Thiokol, Inc.,* and *Du Pont*, the New Mexico Supreme Court in *Conoco, Inc.*, 1997-NMSC-005, ¶13, stated that because of the similarity between Iowa and Rhode Island's tax scheme, "New Mexico's tax scheme violates the Foreign Commerce Clause unless saved by the Detroit Formula." As the New Mexico Supreme Court explained,

> [t]he Detroit formula, named after an agreement between the Ford Motor Company and the city of Detroit, operates to reduce the New Mexico taxable income base by adding into the denominators of the parent corporation's property, payroll, and sales a portion of the property, payroll, and sales of dividend-producing foreign subsidiaries. This

> portion is determined by dividing the net dividends the parent corporation receives from foreign subsidiaries by these subsidiaries' total net profit. This addition into the divisors lowers the fractional multiplier used against a taxpayer's total income, which lowers its New Mexico taxable income base.

Id. ¶14 (internal citations excluded).

The Court rejected the Department's argument that the Detroit Formula remedied the disparate treatment of foreign and domestic dividends because the Detroit Formula "does not eliminate dividends paid by foreign subsidiaries in every case," including for the two taxpayers at issues in *Conoco, Inc*. *Id*. at ¶15. The Court ultimately held that "the taxing of dividends *under the separate corporate entity method* is unconstitutional, even with the Detroit Formula." *Id.* at 16 (emphasis added).

Thus, in New Mexico, under the separate corporate entity method, the Department may not tax a corporation's foreign subsidiary dividend income without running afoul of the Foreign Commerce Clause, as articulated in *Kraft* and *Conoco, Inc*. And if Taxpayer filed it return under the separate corporate entity method, the Department could not tax the foreign subsidiaries dividend income pursuant to the holding of *Kraft* and *Conoco, Inc*. *See also* Department Regulation 3.4.1.12 NMAC (1998). But the *Conoco, Inc.* decision of the Supreme Court was silent as to the constitutionality of New Mexico's consolidated group method and the combined return method at issue in this protest.

Two other New Mexico cases have considered and rejected Foreign Commerce Clause challenges to New Mexico's combined return method. In one case, *NCR Corp*, 1993-NMCA-060, ¶5, the New Mexico Court of Appeals considered a Foreign Commerce Clause challenge to the Department's standard three-factor formulary apportionment of NCR's unitary business income. Critical to the Court of Appeals' ultimate holding in the case was the fact that NCR, a domestic company doing business in New Mexico, was found to have a unitary business relationship with the foreign subsidiaries that generated unitary income for NCR. *See NCR Corp.*, 1993-NMCA-060, ¶20. As the Court of Appeals aptly explained, "[t]he tax in question is not a tax on any of NCR's foreign subsidiaries; instead, the tax falls upon an apportioned share of NCR's income which it receives in the form of royalties, interest, and dividends from its unitary foreign subsidiaries." *Id.*

Because the tax fell on an apportioned share of unitary business income of a domestic corporation engaged in business in New Mexico, the New Mexico Court of Appeals found that the tax was not a tax on the foreign subsidiaries and did not run afoul of the Foreign Commerce Clause. *See id*. As the Court of Appeals explained,

> Contrary to the contentions of NCR, in the instant case, New Mexico is taxing only an apportioned share of the income of NCR, a domestic corporation, not imposing a tax on tangible property of a foreign corporation. Unlike the situation in *Japan Line*, multiple taxation, although real, is not inevitable, the tax was fairly apportioned under the formula set forth in UDITPA, and the legal incidence of the tax here does not fall on a foreign owner but instead is upon a unitary, domestic entity.

Id.

Building on *NCR Corp.* is the *Xerox* administrative decision and order of Hearing Officer Margaret Alcock, issued by the Administrative Hearings Office's precursor entity, the Department's Hearings Bureau. *See Xerox*, 2003 WL 24889474 (non-precedential). Although the administrative decision is non-precedential, Hearing Officer Alcock's well-regarded *Xerox* decision and order is still insightful to the analysis of this protest. *See J. Hellerstein & W. Hellerstein*, ¶4.21[1][d] (in perhaps the preeminent authority on state and local taxation, the hearing officer's *Xerox* opinion is cited for its thoughtfulness). The hearing officer cited favorably both *Morton Thiokol, Inc.'s* and *Du Pont's* rejection of the application of Foreign Commerce Clause under *Kraft* to the combined filing schemes in Kansas and Maine respectively. *See Xerox*, 2003 WL

24889474, 8-10 (non-precedential). The hearing officer noted that the holding of *Conoco, Inc.* was limited to separate corporate entity method filers. *See Xerox*, 2003 WL 24889474, 10 (non-precedential).

Hearing Officer Alcock then addressed the New Mexico Court of Appeals decision in *NCR Corp.*, noting that the Court had allowed taxation of a corporate taxpayer's foreign-source income over a Foreign Commerce Clause challenge because the income was derived from the subsidiaries of a fully-integrated unitary business and New Mexico only taxed an apportioned share of the corporation's total unitary business income. *Xerox*, 2003 WL 24889474, 11-12 (non-precedential); *See also NCR Corp.*, 1993-NMCA-060, ¶20. In an important passage, Hearing Officer Alcock found that "[u]nder the combined filing method (and in contrast to the separate filing method discussed in *Conoco, Inc.*), Xerox was also required to include on its [combined] return the income of any domestic subsidiaries that were part of Xerox's unitary business." *Xerox*, 2003 WL 24889474, 12 (non-precedential). In other words, through the unitary business lens underpinning the combined reporting method, Xerox was compelled to include the dividends of any unitary subsidiary—foreign or domestic—in its taxable income. The dividing line for disparate treatment was not between foreign and domestic subsidiaries of Xerox, but between unitary and non-unitary subsidiaries. *See Xerox*, 2003 WL 24889474, 16-18 (non-precedential). Because of this equal treatment of all subsidiaries premised under the unitary business principal rather than on location of the subsidiary, the hearing officer found that New Mexico's combined reporting scheme as applied to Xerox had not violated the Foreign Commerce Clause. *See Xerox*, 2003 WL 24889474, 18 (non-precedential).

In *Xerox*, the Department had also employed the Detroit Formula to provide factor relief by adding representation of the activities of the foreign subsidiary that produced the unitary income, even though the hearing officer indicated that *NCR Corp*. held that no such relief was required. *See Xerox*, 2003 WL 24889474, 13 (non-precedential). Nevertheless, including some foreign factor relief was an important part of New Mexico providing substantial equity in treatment for combined filers, as Hellerstein and Hellerstein noted in commenting positively on the *Xerox* decision:

> New Mexico had, in principle at least, **provided substantial equality** between income from unitary foreign and domestic subsidiaries **by including the income in the apportionable tax base** (whether in the form of dividends or through combination) **and by providing representation of the subsidiaries' factors in the formula** employed to apportion such income.

J. Hellerstein & W. Hellerstein, ¶4.21[1][d] (emphasis added).

In the absence of presentation of clear and cogent evidence to the contrary, the hearing officer found that Xerox had not met its heavy burden[9] of showing that the apportionment formula employed by the Department was not a fair approximation of that taxpayer's income reasonably related to that taxpayer's in-state activities. *See Xerox*, 2003 WL 24889474, 13 (non-precedential).

Like Kansas (*Morton Thiokol, Inc.)*, Maine (*Du Pont*), and New Mexico (*NCR Corp.* and *Xerox*), many other states have ruled that combined reporting regimes, where an apportioned share of the unitary income of a corporation is subject to tax, do not run afoul of the Foreign Commerce Clause. *See Caterpillar, Inc. v. Comm'r of Revenue*, 568 N.W.2d 695 (Minn. 1997) (the Minnesota Supreme Court found that Minnesota's water's edge combined reporting system, and its accompanying apportionment formula, did not facially discriminate against foreign commerce); *See GE v. Comm'r, N.H. Dep't of Revenue Admin.*, 154 N.H. 457, 914 A.2d 246 (2006) (New Hampshire Supreme Court distinguishing between the separate entity reporting at issue in *Kraft* and New Hampshire's water's edge combined reporting for unitary businesses);

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[9] Citing *Container Corp.*, 463 U.S. 159, 161 (1983). *See also Allied-Signal*, 504 U.S. 768, 782, citing *Exxon Corp.*,447 U.S. 207, 224.

See Agilent Techs. v. Dep't of Revenue of the Colo., 2016 Colo. Dist. LEXIS 1, *15-18 (non-precedential district court decision, finding that Colorado's combined reporting regime does not violate Foreign Commerce Clause). Overall, most of the various states considering some form of combined reporting based on the unitary business principal have found inclusion of apportioned foreign dividend income to not run afoul of the issues addressed by *Kraft* and *Conoco, Inc*.[10]

Pursuant to the holding in *NCR Corp.* and the persuasive rationale in *Xerox*, New Mexico's combined reporting method, where New Mexico imposes an apportioned tax on the unitary corporation's income regardless of the foreign or domestic character of the subsidiary that generated the income, both generally and as applied to this Taxpayer, does not discriminate under the Foreign Commerce Clause. Here, as was previously discussed, the foreign subsidiaries in question were unitary with Taxpayer and their unitary business income is includable in Taxpayer's income for purposes determining New Mexico's apportioned share of taxable income.

Through the unitary business lens underpinning the combined reporting method, a taxpayer is compelled to include the income of any unitary subsidiary—foreign or domestic—in its taxable income. The dividing line for disparate treatment is not between foreign and domestic subsidiaries but between unitary and non-unitary subsidiaries. This tax symmetry between unitary foreign or domestic subsidiary income does not run afoul of the Foreign Commerce Clause. *See Du Pont*, 675 A.2d 82, 88 (although domestic dividends paid to parent corporation are deducted, the apportioned income of the domestic subsidiaries is subject to tax, leading to tax symmetry); *See also NCR Corp.,* 1993-NMCA-060; *See also Xerox*, 2003 WL 24889474 (non-

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[10] An exception is Ohio, where the Ohio Supreme Court found that the state's combined reporting statute was unconstitutional under the rationale of *Kraft*. *See Emerson Elec. Co. v. Tracy*, 90 Ohio St. 3d 157, 735 N.E.2d 445, 2000-Ohio-17.

precedential)*; See also Morton Thiokol, Inc.*, 254 Kan. 23. It is that tax symmetry that Hellerstein and Hellerstein recognized in highlighting the non-precedential yet persuasive *Xerox* decision. *See J. Hellerstein & W. Hellerstein*, ¶4.21[1][d]. Indeed, the New Mexico Supreme Court in *Conoco, Inc.* recognized the distinguishing factor between a constitutional scheme and the single filer scheme violative of the Foreign Commerce Clause was the presence of the tax symmetry identified in *Thiokol* and *Du Pont*. *See Conoco, Inc.*, 1997-NMSC-005, ¶ 12. Under this same rationale, there is no foreign commerce clause violation in this case, where Taxpayer filed a combined return listing all unitary income from both foreign and domestic subsidiaries on its return and New Mexico only seeks to tax its apportioned shared of Taxpayer's unitary income.

Issue Five: Taxpayer's Equal Protection Claim Fails.

Related to Taxpayer's challenge under the Foreign Commerce Clause, Taxpayer also asserts that the Department's assessment and proposed alternative apportionment methods violate the Equal Protection Clause under the state and federal constitutions for two reasons. Taxpayer first argues that New Mexico disfavors foreign subsidiaries in calculating tax liability because there is no foreign factor representation. For its second equal protection challenge, Taxpayer argues that New Mexico favors separate entity filers over combined return filers because, pursuant to *Kraft* and *Conoco, Inc.*, New Mexico provides a foreign dividend exclusion to separate entity filers. Taxpayer also suggests that New Mexico's Equal Protection Clause provides broader protections than the federal Equal Protection Clause. Both of Taxpayer's arguments touch partially on issues largely rejected in Foreign Commerce Clause challenge discussed above, and there is no need to fully repeat that analysis again in this section.

Even beyond that previous discussion, Taxpayer's Equal Protection claim remains unpersuasive. The United State Supreme Court has long afforded the legislature broad discretion in imposing taxation on different classes of taxpayers. As the United States Supreme Court aptly stated in 1940,

> [t]he broad discretion as to classification possessed by a legislature in the field of taxation has long been recognized. This [Supreme] Court fifty years ago concluded that 'the fourteenth amendment was not intended to compel the states 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… [I]n taxation, even more than in other fields, legislatures possess the greatest freedom in classification… [T]he presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is a hostile and oppressive discrimination against particular persons and classes. The burden is on the one attacking the legislative arrangement to negate every conceivable basis which might support it.

Madden v. Commonwealth of Kentucky, 309 U.S. 83, 87-88 (1940).

The New Mexico Supreme Court adopted this same standard in considering equal protection challenges to tax classifications under both the federal and state constitutions. *See Michael J. Maloof & Co. v. Bureau of Revenue*, 80 N.M. 485, 458 P.2d 89 (1969) (quoting *Madden* and applying that standard to an equal protection challenge to differential tax treatment under the federal and state constitution).

Taxpayer suggests in its written closing argument that the New Mexico Constitution's Equal Protection Clause requires an additional governmental justification for distinguishing between classes beyond the traditional rational basis analysis used for all equal protection claims not involving protected classes or fundamental personal rights. In support of its argument, Taxpayer cites a Worker's Compensation Act case where the court found there was no rational basis to differentiate between farm/ranch laborers and other laborers other than arbitrary discrimination. *See*

Rodriguez v. Brand W. Dairy, 2016-NMSC-029, ¶ 2, 378 P.3d 13, 17–18. Taxpayer's citation does not support its suggestion of an elevated equal protection standard under the state constitution for two reasons. First, *Rodriguez* in fact reaffirms that the rational basis standard is the appropriate level of scrutiny for economic legislation (like tax statutes) that does not touch on sensitive, protected classes or fundamental rights. *See id*. ¶22. Secondly, in the tax context, case law makes clear that there is no elevated standard for an equal protection analysis under the state constitution beyond the rational basis for the classification employed under the federal constitution. *See J. Maloof*, 80 N.M. 485.

In New Mexico's tax jurisprudence, the Equal Protection Clause of the state and federal constitutions, as well as the state constitution's tax uniformity provision, have been applied similarly. *See Anaconda Co. v. Prop. Tax Dept.*, 1979-NMCA-158, ¶¶ 22-23, 94 N.M. 202, 210. When considering a tax statute under the Equal Protection Clause of both the state and federal constitution, our Court of Appeals has stated that "[c]onsidering the broad power of the legislature to classify for tax purposes, and the presumption of the constitutionality of the tax, *any reasonable justification* for the classification is sufficient to sustain its constitutionality." *Id*., 1979-NMCA-158, ¶24 (emphasis added). *See also Pinghua Zhao v. Montoya*, 2014-NMSC-025, ¶ 19, 329 P.3d 676, 682 (Legislature has greatest freedom in classifications for tax purposes and courts will use every presumption in favor of validity of a tax classification).

Under that standard, Taxpayer fails to establish any equal protection violation in this case. As Taxpayer acknowledges, creation of the foreign dividend deduction for separate entity filers was necessary considering the United States Supreme Court's *Kraft* decision and the New Mexico Supreme Court's decision in *Conoco, Inc.* That distinction is reasonably justified as necessary to ensure that the separate entity filer statutory scheme remains constitutional. *See Anaconda Co.*, 1979-NMCA-158, ¶¶22-23 (presumption of the constitutionality of the tax).

Regarding combined filers' inability to get a similar deduction, there is a rational, non-discriminatory basis for that as well: the state distinction is not premised on whether the subsidiary is foreign or domestic but whether the subsidiary is unitary or non-unitary. In one manner or another, under the combined reporting method, the income of any unitary subsidiary (be it foreign or domestic) is included in the combined return. Additionally, as discussed in the alternative apportionment section, the Department is affording Taxpayer foreign factor relief in calculating tax liability in this case both under the 30% exclusion method and the Detroit Formula. As Hellerstein and Hellerstein stated in positively commenting on the *Xerox* decision and order, by including unitary income from both foreign and domestic subsidiaries in one form or another and in providing foreign factor relief, New Mexico provides substantial equity to combined return filers. *J. Hellerstein & W. Hellerstein*, ¶4.21[1][d].

To say there is no rational basis for a combined reporting system premised on the distinction between unitary and nonunitary business income would require rejection of the unitary business principal. Without reiterating the case law discussed in the unitary business section, it is sufficient to say the long progression of constitutional tax jurisprudence illustrates that the unitary business principal—that a state may tax an apportioned share of a unitary business enterprise income—is entirely rational and constitutional. The Legislature clearly had a rational basis in implementing a distinction for tax treatment purposes between unitary and nonunitary corporations as well as between separate entity files and combined return filers. Therefore, there is no equal protection violation in this case under either the state or federal constitutions.

Issue Six: Department's 30% Exclusion Method is the Appropriate Apportionment Method.

In this case, when Taxpayer failed to respond to the request for additional supporting documentation, the Department issued its assessment using the information Taxpayer had provided on the CIT-1 return, including relying on the standard three factor apportionment method. Taxpayer argued that the final original assessment in this case resulted in impermissible and unconstitutional distortion. Because of this distortion, Taxpayer proposed two alternative apportionment methods in this case. The Department's corporate income tax witness Mr. Armer acknowledged during testimony that the Department's original assessment needed to be corrected to address obvious distortion related to accumulated foreign dividends without foreign factor relief. That said, the Department argues that any distortion in the original assessment stemmed from Taxpayer's lack of cooperation and production of information in a timely fashion both before the assessment and throughout the protest process, and to that extent, the Department argues the protest should be summarily denied. But in the alternative, the Department proposed its own alternative apportionment methods to correct the distortion observed by Mr. Armer.

To resolve this issue, the hearing officer will first provide an overview of apportionment, including addressing the burden necessary in showing unconstitutional distortion under standard apportionment and in subsequently establishing the reasonableness of a proposed alternative apportionment method. Next, the hearing officer will address the acknowledged, obvious distortion under the standard three factor apportionment method. Finally, the hearing officer will review each party's proposed alternative apportionment methods in turn.

a. *Overview of Apportionment, Distortion, and Alternative Methods of Apportionment.*

States may tax a fairly apportioned share of a multistate entity's business income. *See Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 458-462 (1959). New

Mexico, like many states, has adopted the Uniform Division of Income for Tax Purposes Act ("UDITPA") to address fair apportionment and allocation of income earned by multistate or multinational entities for their New Mexico activities. *See* NMSA 1978, §§7-4-1 through 7-4-21; *see also ASARCO Inc.*, 458 U.S. 307, 311 fn.3 (short discussion of the history of UDITPA); *see also J. Hellerstein & W. Hellerstein*, State Taxation, ¶9.01 (3rd ed. 2001-2015) (discussion of the history of adoption of UDITPA, or similar statutory regimes, by numerous states).

Under UDITPA, business income is apportioned according to a three-factor formula based on the amount of a corporation's respective property, payroll, and sales everywhere (the denominators) against the respective amount of its property, payroll, and sales within a state (the numerators). Using the denominator and numerator in each category of property, payroll, and sales, a percentage is calculated for each of the three factors, and the average percentage of the three is then applied against the corporation's total income to determine the percentage amount of apportioned income subject to New Mexico's corporate income tax. *See* NMSA 1978, §§ 7-4-10 through 7-4-18.

The general idea behind UDITPA, amongst others, is to ensure that each state only taxes an apportioned share of a taxpayer's income, a share under the formula roughly commensurate with the portion of the income attributable to the business activities conducted within that respective state. *See e.g. Kmart Props., Inc. v. Taxation & Revenue Dep't (KPI),* 2006-NMCA-026, ¶ 46, 139 N.M. 177 (New Mexico Court of Appeals provides a brief overview of the apportionment process under UDITPA and describes that process as "an effort at fair and uniform allocation of taxable income among the states."), *rev'd on other grounds and certiorari as to corporate income tax issues quashed, Kmart Corp. v. Taxation & Revenue Dep't.*, 2006-NMSC-006, 139 N.M. 172. UDITPA has two basic goals: "(1) fair apportionment of income among the taxing jurisdictions; and

(2) uniformity of application of the statutes." *Twentieth Century-Fox Film Corp. v. Dep't of Revenue*, 299 Or. 220, 227, 700 P.2d 1035 (1985)[11]. If all states applied the UDITPA formula in a uniform manner, then 100% of a multistate taxpayer's income, and "no more or no less," would be subject to tax. W.J. Pierce, *The Uniform Division of Income for State Tax Purposes*, 35 Taxes 747, 748 (1957), (as cited in *Twentieth Century-Fox Film Corp.*, 299 Or. 220, 226-27).

Although not the only permissible method of apportionment, UDITPA's standard three-factor formulary apportionment was the historical "benchmark" for fair apportionment. *Container Corp.***,** 463 U.S. 159, 170. As the United States Supreme Court noted, the reason UDITPA's standard three-factor apportionment has become the approved standard is that "payroll, property, and sales appear in combination to reflect a very large share of the activities by which value is generated." *Container Corp.,* 463 U.S. 159, 183. While there is expected variance between the three factors, the average of the three factors is designed in most cases to arrive at a reasonably reliable determination of a taxpayer's activities in a state. Thus, the three-factor apportionment, even if such formula is "necessarily imperfect," is generally able to avoid the "sort of distortions" that raise constitutional issues with state taxation of multistate businesses. *Id*.

While *Container Corp.* embraced the standard three-factor formulary apportionment, the Supreme Court also established in that decision that any apportionment formula used must be both internally and externally consistent. *See Container Corp.*, 463 U.S. 159, 169-170. By internal consistency, the Court meant that "the formula must be such that, if applied by every

[11] The hearing officer generally agrees with Taxpayer's footnote 14 in its closing argument, which points out that most states have moved away from the uniformity value of UDITPA's standard three-factor formulary apportionment in favor of alternative apportionment methods that rely more heavily on the sales factor, including double-weighing that factor, in the apportionment formula. Nevertheless, the applicable New Mexico statute established the traditional, three-factor standard apportionment formula as the default apportionment for a 2015 corporate income tax return. Therefore, the historical purpose and evolution of three factor standard apportionment remains important in analyzing the legal disputes in this protest.

jurisdiction, it would result in no more than all of the unitary business' income being taxed." *Id.,* 463 U.S. at 169.

The Supreme Court identified external consistency as a much more difficult concept: "the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated." *Id*. As the New Jersey Supreme Court, in synthesizing various United Supreme Court cases addressing external consistency, summarized

> [e]xternal consistency looks "to the economic justification for the State's claim upon the value taxed, to discover whether a State's tax reaches beyond that portion of value that is fairly attributable to economic activity within the taxing State." [*Okla. Tax Comm'n v. Jefferson Lines*, 514 U.S. 175, 185 (1995)] Stated simply, the question is whether the state's tax law reasonably reflects the activity within its jurisdiction. The external consistency test requires a "practical inquiry" into the inter-state activity taxed in relation to the activity in the taxing jurisdiction. *Goldberg v. Sweet*, 488 U.S. 252, 264-65, 109 S. Ct. 582, 590-91, 102 L. Ed. 2d 607, 618-19 (1989).

Whirlpool Props., Inc. v. Dir., Div. of Taxation, 208 N.J. 141, 165, 26 A.3d 446 (2011).

The United States Supreme Court has indicated that an apportionment formula is not invalidated simply because it may result in the taxation of income earned beyond the taxing state. *See Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 272 (1978). Because apportionment involves "slicing a shadow," reasonable imprecision under an apportionment formula is permitted. *Container Corp.*, 463 U.S. 159, 192-93. An apportionment formula generally only fails when a taxpayer can show by clear and cogent evidence that the income attributed to the state is "out of all appropriate proportions to the business transacted… in that state." *Hans Rees Sons, Inc. v. North Carolina*, 283 U.S. 123, 135 (1931). While the apportionment formula need not be exact, when a taxpayer shows that an application of a formula for apportionment results in gross distortion, a modification to the application of that formula is required in that particular instance. *See Norfolk & W. R. Co. v. Mo. State Tax Comm'n*, 390 U.S. 317, 329 (1968).

UDITPA itself contains a provision that allows for equitable adjustment to the standard three factor apportionment when the three-factor formula does not fairly capture the business activity of a multistate taxpayer. This equitable adjustment provision of UDITPA has been adopted in New Mexico and codified as NMSA 1978, Section 7-4-19. Section 7-4-19 reads:

> If the allocation and apportionment provisions of the Uniform Division of Income for Tax Purposes Act [7-4-1 NMSA 1978] do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for, or the department may require, in respect to all or any part of the taxpayer's business activity, if reasonable:
>
> A. separate accounting;
> B. the exclusion of any one or more of the factors;
> C. the inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or
> D. the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

UDITPA was designed primarily to address manufacturing and merchandising. *See Twentieth Century-Fox Film Corp.*, 299 Or. 220, 227. The drafters of UDITPA created this equitable apportionment provision to provide flexibility to tax administrators and taxpayers when the standard three-factor apportionment would reach an "unreasonable result." W.J. Pierce, *The Uniform Division of Income for State Tax Purposes*, 35 Taxes 747, 781 (1957), as cited in *Twentieth Century-Fox Film Corp.*, 299 Or. 220, 227, 700 P.2d 1035. As Professor Pierce, the drafter of UDITPA expounded, the equitable apportionment provision of UDITPA allows for

> some latitude for showing that for the particular business activity, some more equitable method of allocation and apportionment could be achieved. Of course, departures from the basic formula should be avoided except where reasonableness requires. Nonetheless, some alternative method must be available to handle the constitutional problem as well as the unusual cases, because no statutory pattern could ever resolve satisfactorily the problem for the multitude of taxpayers with individual business characteristics.

W.J. Pierce, *The Uniform Division of Income for State Tax Purposes*, 35 Taxes 747, 781 (1957), as cited in *Twentieth Century-Fox Film Corp.*, 299 Or. 220, 226-227, 700 P.2d 1035.

The party seeking to depart from the standard apportionment formula carries the burden of persuasion as to why the modification is necessary. *See KPI*, 2006-NMCA-026, ¶¶ 50-51. In order to meet this burden of departure, the party seeking the departure must prove two things: first, that the statutory formula as a whole does not fairly represent the extent of the taxpayer's business activity in the state and second that the alternative method of apportionment employed is reasonable. *See Twentieth Century-Fox Film Corp.*, 299 Or. 220, 233, 700 P.2d 1035 (1985).

Taxpayer avers in its closing argument that in New Mexico, the party seeking to depart from the standard apportionment need only establish that there is distortion by the preponderance standard rather than the heavier clear and cogent evidence standard articulated in other non-precedential Administrative Hearings Office decisions. As support for its argument, Taxpayer cites Regulation 22.600.1.18 (A) NMAC (establishing the preponderance standard as the default standard unless a statute specifies otherwise), the absence of a statutory standard under Section 7-4-19's equitable apportionment provision, and various cases from other jurisdictions showing that some states only require proof by the preponderance. The hearing officer does not agree with Taxpayer's argument that in New Mexico, the party seeking the departure from the standard, three-factor formulary apportionment need only prove distortion by the preponderance of the evidence.

Instead, under applicable federal and New Mexico jurisprudence, the party seeking to deviate from standard apportionment must demonstrate distortion by clear and cogent evidence. Three cases in New Mexico make clear that under the UDITPA framework, deviations from the standard apportionment formula require more than a simple, more-likely-than-not preponderance standard. Although reversed by the United States Supreme Court on unitary grounds, the New

Mexico Supreme Court (as Taxpayer even acknowledges) adopted the clear and cogent evidence standard for those seeking to deviate from the standard formulary apportionment. *See Taxation & Revenue Dept. of State of N. M. v. F. W. Woolworth Co.*, 1981-NMSC-008, ¶ 54, 95 N.M. 519, 530, rev'd, *F. W. Woolworth Co. v*, 458 U.S. 354 (1982).

The New Mexico Court of Appeals also adopted the clear and cogent evidence standard in *NCR Corp.*: "[a]s noted in *Container Corp*., a taxpayer seeking to invalidate a state's apportionment formula *must show by clear and cogent evidence* that the income attributed to the state is in fact disproportionate to the business transacted in that state." 1993-NMCA-060, ¶ 38 (emphasis added). The Court of Appeals in KPI also found that deviations from the "standard formula should be an exception, not the rule," but that in that case, the Department had shown "exceptional circumstances" justifying a departure. *KPI*, ¶ 51. Although *KPI* did not expressly reference an evidentiary standard vis-à-vis deviations from formulary apportionment, the rarity and exceptional grounds rationale articulated by the Court of Appeals is closer to the elevated clear and cogent standard than the preponderance standard. This body of New Mexico state case law is also consistent with federal jurisprudence in this realm. *See Container Corp*., 463 U.S. 159, 179-181; *see also Moorman Mfg. Co.*, 437 U.S. 267 (1978).

a. Application of Standard Three-Factor Apportionment Formula is Distortive.

Even under the elevated clear and convincing evidence standard in this case, Taxpayer established that application of the three-factor standard apportionment in this case leads to significant distortion. While the Department blames Taxpayer's lack of cooperation and production of information for the distortion, the Department does not vigorously contest that the original assessment contained obvious distortion that needed to be corrected. Indeed, Department Corporate Tax specialist Mr. Armer acknowledged during testimony that the original assessment contained obvious distortion. Given this de facto concession and Taxpayer's meeting the presumption of correctness as to the original assessed amount, this decision will only provide a quick summary of why the standard three-factor apportionment formula in this case is distortive and why an alternative apportionment method is required.

The obvious distortion stems from two related shortcomings in the assessment (and the hearing officer agrees with the Department that Taxpayer bears some of the burden for these shortcomings by not providing the requested follow up information). First, as Taxpayer persuasively argues, the Department provided no foreign-factor relief in applying the standard three factor apportionment formula despite the heavy presence of Taxpayer's unitary foreign subsidiary income. By simply including Taxpayer's unitary foreign source dividends in the Taxpayer's United States property, payroll, and sales factors, the standard apportionment method does not reflect Taxpayer's foreign activities in determining what percentage of the unitary income might accurately reflect the extent of Taxpayer's business in New Mexico. Not only does the absence of foreign factor relief lead to distortion in the original assessment, it also is contrary to the important element of the *Xerox* decision that Hellerstein and Hellerstein praised as part of the reason why New Mexico provided substantial equity in its treatment of unitary domestic and foreign subsidiaries under the combined reporting method[12]. *See J. Hellerstein & W. Hellerstein*, ¶4.21[1][d].

Second, the assessment was largely premised on dividend income accumulated over approximately two decades. By applying only the current year's factors to this accumulated income without any knowledge about consistency of previous years' factors, there is some distortion which Taxpayer demonstrated and the Department acknowledged during testimony. Therefore, because of

[12] The New Mexico Court of Appeals did not find the absence of foreign factor relief in the apportionment formula to be of concern in *NCR Corp.*, 1993-NMCA-060, ¶35-36. However, it does not appear there was an admission by the Department in *NCR Corp.* of obvious distortion under the apportionment formula as there is in the present protest.

the obvious distortion shown by Taxpayer and acknowledged by the Department, the standard formulary apportionment method in this case requires modification under UDITPA and the case law addressed above. *See* § 7-4-19; *See also KPI*, 2006-NMCA-026, ¶¶ 50-51.

b. Taxpayer's proposed alternative methods are not reasonable.

While the standard, formulary apportionment does not fairly represent Taxpayer's business activities in this case, the party seeking to depart from the standard apportionment must also show that the alternative method of apportionment is reasonable. *See Twentieth Century-Fox Film Corp.*, 299 Or. 220, 233, 700 P.2d 1035, 1044. To establish reasonableness of the proposed alternative method, the party must show that the proposed alternative apportionment method achieves three things: first, that it fairly represents business activity; second, that it does interfere with uniformity for purposes of UDITPA; and third, that it reflects the economic reality of business activity within the state. *See id*.

In this case, Taxpayer proffers two alternative apportionment methods. Both Taxpayer's offered alternatives fail the three reasonableness requirements for an alternative apportionment method. This is in part because one of the core premises underlying most of Taxpayer's case is erroneous: that Taxpayer's economic activities within the state in 2015 were minimal, generated taxable losses, and did not contribute to generating the disputed foreign source income.

To the contrary, the hearing officer finds that the economic reality of Taxpayer's 2015 New Mexico operations was far more significant to Taxpayer's unitary operations in 2015 (and in the years before when the dividend income was earned) than Taxpayer claims. Even during the period when the unitary foreign subsidiaries accumulated the dividend income, the Permian Basin was one of Taxpayer's main focuses in oil and gas production, fueling Taxpayer's business operations success. Beginning in 1991, the Permian Basin was one of Taxpayer's largest oil production regions, and it remained a focus of Taxpayer from 1991 right through 2015, when it became an even larger part of Taxpayer's production activities.

By Taxpayer's own admissions, it undertook its strategic rebalancing away from its foreign subsidiaries between 2012 and 2015 in order to fund, expand, and focus on Taxpayer's North American operations because North America presented a more stable and consistent source of revenue. As Taxpayer's own annual S.E.C. Form 10-K reports make clear, Taxpayer used the proceeds of sales of the foreign assets and subsidiaries to grow its North American profile. One of the main stars of that expansion during the rebalancing, according to Taxpayer's filings, was Taxpayer's Permian Basin operations. In 2013, Taxpayer stated that the Permian and Anadarko Basins allowed it momentum in increasing North American oil and gas production. In both 2014 and 2015, the Permian Basin accounted for approximately one third of Taxpayer's total worldwide liquid oil and gas production, making it the largest region of Taxpayer's production in both North America and the world.

Taxpayer's assertion that its New Mexico economic activities were minimal because of its book losses in New Mexico is inconsistent with the economic reality of the significant value that the Permian Basin production played in Taxpayer's oil and gas unitary business enterprise in 2015, where the Permian Basin accounted for one third of Taxpayer's total worldwide oil and gas production. The commonsense, economic reality is that Taxpayer relied on access to New Mexico's portion of the Permian Basin to get a plurality of the product that is at the heart of Taxpayer's business operations in North America. And any alternative apportionment that does not recognize that important economic reality fails the first and third factors of the alternative apportionment reasonableness test set forth in *Twentieth Century-Fox Film Corp.*, 299 Or. 220, 233, 700 P.2d 1035, 1044. Nor would any alternative apportionment that does not recognize that important economic reality be consistent with New Mexico case law direction to interpret the UDTIPA provisions in a manner effectuating fair taxation of a multistate corporation engaged in business activities in the state. *See Pub. Serv. Co. of N.M. v. N.M. Taxation & Revenue Dept.*, 2007-NMCA-050, ¶ 33, 141 N.M. 520, 529–30, 157 P.3d 85, 94–95.

Taxpayer's first proposed alternative method is the 965-concept method. Under this method, Taxpayer seeks to employ the Department's 965 bulletin method for treatment of the mandatory repatriation of undistributed foreign income under the federal Tax Cuts and Jobs Act (TCJA) of 2017. *See PL 115-97*, December 22, 2017, 131 Stat 2054. Under the TCJA, by way of amendments made to 26 U.S.C. § 965 (Section 965), taxpayers were required to pay a one-time tax on any of taxpayer's controlled foreign corporations untaxed dividends earned between January 1, 1987, and December 31, 2017, as part of that taxpayer's Subpart F income. *See* 26 U.S.C. § 965; *see also PL 115-97 (Sec. 14103)*. In the realm of tax practitioners and tax academics, this one-time repatriation of untaxed foreign dividend income under the TCJA has been commonly referred to as the transition tax pursuant to Section 965(C).

After passage of the TCJA, the Department engaged in high-level policy discussions to determine how New Mexico would treat income generated under Section 965(C)'s transition tax on accumulated foreign dividend income. The Department ultimately settled on the approach articulated by Department Bulletin B-300.17. *See* Taxpayer Ex. #14. Under that Department Bulletin, in order to avoid the complexity and onerous record-keeping challenges of determining foreign factors for income accrued over long periods of time, the Department determined that "New Mexico will permit a taxpayer to exclude 30 percent of their net IRC 965 deferred foreign income from their taxable income." *Id*.

It is this Department Bulletin B-300.17 approach that Taxpayer proposes as its alternative apportionment method, the 965 concept method. Taxpayer argues that the facts of its protest are analogous to the TCJA's transaction tax. Therefore, Taxpayer argues that the Department's 965 treatment is an appropriate and reasonable alternative apportionment method. While the hearing officer does understand the similarity between accumulated foreign dividends under both scenarios, the hearing officer is not persuaded that the situations are otherwise analogous. The problem is that both the TCJA transition tax and the Department's Bulletin B-300.17 only apply to one specific, forced deemed dividend repatriation in 2017 versus the elective deferral decisions and then subsequent elective repatriation of the foreign dividends and liquidation of some of the foreign entities by Taxpayer in 2015. Unlike taxpayers impacted by the one-time deemed dividend repatriation under the TCJA in 2017, Taxpayer made the voluntary business decision a few years before passage of the TCJA to strategically rebalance its business away from its foreign subsidiaries towards its North American operations (including in New Mexico's Permian Basin). The TCJA's deemed repatriation was imposed on all corporations regardless of their strategic needs, business decisions, or ability to plan for the dividend repatriation. In that sense, the Department reasonably provided some additional specific relief under that unique TCJA fact pattern to taxpayers in 2017 because those affected taxpayers had no ability to plan, prepare, or otherwise determine a course of action on the accumulated foreign deferred earnings. But Taxpayer was not in the same situation as those 2017 taxpayers impacted by the deemed dividend repatriation because Taxpayer had the ability to make its own strategic and business-based decision a few years in advance, and carefully plan out how and when the disposition would proceed.

Indeed, twice on the first page of Department Bulletin B-300.17, the Department makes clear that the bulletin is only applicable to TCJA's 2017 deemed dividend repatriation. First, the bulletin states that it "applies only to taxpayers liable for New Mexico Corporate Income Tax who are required by Internal Revenue Code (IRC) Section 965 to pay a *transition tax* on the untaxed foreign earnings of certain foreign corporations. Generally, Section 965 requirements only apply to tax year 2017." Second, the bulletin states that it "…addresses only the changes to New Mexico taxable income pursuant to Section 14103 of the TCJA pertaining to a *one-time inclusion in tax year 2017* of certain untaxed foreign earnings and profits…" Taxpayer Exhibit #14.1 (emphasis added). Department Bulletin B-300.17 was designed specifically to ease the onerous recordkeeping concerns related to the mandatory transition tax forced on all taxpayers in 2017, not to other taxpayers in previous years who made elective, strategic, and planned business decisions related to foreign dividend income.

The hearing officer does not find using Department Bulletin B-300.17, designed for a specific and unique deemed dividend repatriation transition tax in one specific tax year, a reasonable alternative apportionment method related to Taxpayer's business activities in 2015. Taxpayer has not presented compelling evidence that Department Bulletin B-300.17, designed for a different tax year and addressing a forced repatriation, fairly reflects Taxpayer's strategic and voluntary business activities in 2015. Nor has Taxpayer shown that it has used or attempted to use this approach uniformly or how this concept would impact uniformity in other UDITPA jurisdictions.

As the Department persuasively argues, Taxpayer made the decision to defer the foreign income for many years for its own reasons and its own purposes. Taxpayer could have taken the dividends each year beginning in 1991 and paid the corresponding corporate tax obligations consistent with the specific business activities, apportionment, and allocation in each respective year. However, for its own reasons and purposes, Taxpayer instead chose to let the dividends accumulate from 1991 through the 2015 tax year. Similarly, Taxpayer made the decision to move away from the foreign subsidiaries to the more stable North American market for its own business reasons and purposes, and on its own schedule. This is in stark contrast to the forced, deemed repatriation under the TCJA applicable to all United States' taxpayers, regardless of those taxpayers' specific business choices, needs, or business plan.

The hearing officer also is not convinced that Taxpayer's Maine Methodology is a reasonable alternative apportionment method. Like New Mexico, Maine includes foreign dividends on a combined return while applying an alternative apportionment method for the foreign income inclusion under the Augusta Formula. *See Du Pont*, 675 A.2d 82 (Me. 1996). Rather than using the Augusta Formula applied against the transition tax income under the TCJA in 2017, Taxpayer asserts that Maine instead provided an 80% exclusion to gross deferred foreign income in that tax year. Taxpayer argued that, given the similarities between Maine's and New Mexico's corporate income tax regimes, Maine's special treatment of the 2017 transition tax income under the TCJA provides a reasonable alternative apportionment for Taxpayer's 2015 New Mexico corporate income tax. However, for the same reasons already discussed in relation to the 965-concept method, the hearing officer is not persuaded that the Taxpayer's proposed Maine Methodology is a reasonable alternative apportionment in this case.

While Taxpayer argues that these alternative approaches, essentially resulting in zero or near zero New Mexico corporate income tax liability, would fairly reflect the extent of Taxpayer's New Mexico activities, as discussed above, the hearing officer is simply not convinced that a near zero corporate income tax liability is reasonably reflective of the true economic reality of Taxpayer's New Mexico business activities given the importance of the Permian Basin in Taxpayer's North American oil and gas production in years up to and including 2015. Whether or not Taxpayer's entities doing business in New Mexico produced book income in New Mexico in 2015, there is little doubt that Taxpayer's unitary business operations received significant business benefit and income through its oil and gas production within New Mexico's portion of the Permian Basin. Indeed, Taxpayer generated one third of its total worldwide liquid gas product from the Permian Basin. There is little reasonableness in any alternative apportionment method that results in essentially zero tax liability in a state that helped Taxpayer produce approximately one third of its entire worldwide oil and gas product in the years leading up to and including 2015. Since the Permian Basin played an important part of Taxpayer's unitary business during the entire period in which the foreign income accumulated and during a period when Taxpayer did not need from a business perspective to pay out those dividends, that rationale also extends to any alternative method seeking to correct the distortion attributable to an extended period of dividends accumulation.

Given the reality of the importance of the Permian Basin to Taxpayer's overall North American oil and gas development business enterprise both during the period when the dividends accumulated and in 2015, it is fair for New Mexico to impose a corporate income tax on a proportioned share of Taxpayer's unitary line of business because the tax bears some relation to Taxpayer's presence and activities in the state. *See Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 625–29 (1981) (finding that the relevant inquiry under the fourth *Complete Auto Transit* of whether the tax is proportionate to the taxpayer's activities in the state is not a mathematical comparison between the extent of a taxpayer's activity in a state versus the value provided by the state, but a question of whether a taxpayer's activities within the state benefitted from the state protections provided). *See also Pub. Serv. Co. of N.M.,* 2007-NMCA-050, ¶ 33.

c. The Department's 30% exclusion rule is the most reasonable of all the proposed alternative apportionment methods.

The Department, recognizing the obvious distortion in the standard apportionment method, offers two alternative apportionment methods in this protest, one of which the hearing officer finds reasonable under the circumstances of this protest.

The first alternative method that the Department offers is the Detroit Formula, foreign factor relief. Under that method, the Department proposed using (with review and verification of Taxpayer's workpapers) the Detroit Formula's factor ratio of 4.0947% rather than the higher factor ratio used under the original assessment of 5.7911%. This approach is consistent with the apportionment method for a combined filer upheld in the well-regarded *Xerox* decision and order. It also makes some headway in addressing the distortion resulting from the failure to include foreign factor relief under the original, standard apportionment in this matter. But despite the Department's argument to the contrary, this alternative method does not do enough to address the distortion of applying a single year's factors against foreign dividends accumulated over an extended, multiyear period. The Department's mathematical proposition that application of a constant factor over an extended period cures any distortion associated with accumulation of deferred income over multiple years depends on the assumption that the formula ratio is consistent from year-to-year[13]. This is problematic because there is no reason to assume a taxpayer-specific consistent factor year over year, for 20-30 years (like at issue in this protest). One would expect some variance from year to year on the ratio over such an extended period. That's why the Department conducted a historical review to determine what is the result, on average, of application of foreign factor relief. The historical review showed that the application of foreign factor relief resulted in an overall average

[13] "If the ratio is a constant, application of UDITPA correctly accounts for deferred income that accrued over multiple years." Department Closing Argument, p. 24.

30% reduction in the taxable income. In that sense, simple application of the Detroit Formula foreign factor relief in one particular year against 20-30 years of accumulated dividends still may not have any bearing on the real economic activity of Taxpayer in those other years. Whereas, applying the average result to the extended period will offset natural variances in activities over that period. This is why Department Corporate Income Tax specialist Mr. Armer noted that standard application of the Detroit Formula would likely not address the distortion under the unique facts of this case and that the Detroit Formula method works functionally better on a year-to-year basis.

Of the four alternative apportionment methods proposed by the parties, the most reasonable approach to address both the foreign factor relief and the accumulated dividend distortion while still being reasonably consistent with the economic reality of Taxpayer's business activities in the state is Mr. Armer's 30% foreign dividend exclusion method. Mr. Armer testified that in the historical experience of the Department, providing foreign factor relief had resulted in a 30% reduction in taxable income. In order to effectuate that practice, Mr. Armer postulated that the distortion issues in this case could be cured by providing a 30% exclusion applied against Taxpayer's deferred foreign income. *See* Dept. Ex. AJ. This application results in a reduction of $4,050,633,570.00 in Taxpayer's 2015 base income compared to the calculation that led to the original assessment. Under this method, Taxpayer would be liable for an additional $12,754,050.00[14] in New Mexico corporate income tax rather than the original assessed corporate income tax principal of $24,187,441.00 or the potential $16,497,121.00 corporate income tax liability under the correct application of the Detroit Formula method.

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[14] Dept. Ex. AJ transposed the NM factor percentage as 5.9711% rather than the correct 5.7911%, which is why there is a discrepancy between the total tax due on that document and the total tax illustrated in the Department's closing argument on p. 25. This amount will also need to be adjusted further to remove the Oil Insurance Limited's nonunitary dividends.

While Mr. Armer had concerns that the Detroit Formula alone was insufficient to cure the distortion related to an extended period of dividend accumulations, as the Department argues in its closing brief, the 30% exclusion method goes beyond the Detroit Formula in correcting that distortion. In absence of more year-by-year specific factor information, applying the historical average of 30% exclusion against a large period of dividend accumulation is likely to better, on average, approximate a taxpayer's annual year-by-year business activity within the state then simply taking one year's relief factor and assuming it applies to all the other years. This is because the Department's historical research shows that foreign factor relief on average results in 30% exclusion. Whereas in any given year in isolation the Detroit Formula may produce a lower or higher relief percentage. Applying the factor relief from a single year in isolation that is either higher or lower than this historical average against a large period of time would exacerbate the distortion in other years that likely fall closer to the historical average. Indeed, in this case the 30% exclusion method against the multiyear accumulated dividends provides a greater reduction of Taxpayer's foreign-source income than application of a single year's correct Detroit Formula yields[15].

Of the proffered alternative apportionment methods, the Department's 30% exclusion method is the only approach before the hearing officer that attempts to reasonably balance the economic reality that Taxpayer's growing activities in New Mexico's Permian Basin, leading up to and including in 2015, helped fuel Taxpayer's unitary business enterprise, while correcting, on average, the distortion related to multi-year accumulated dividends and foreign factor relief. *See Pub. Serv. Co. of N.M.*, 2007-NMCA-050, ¶ 33 (UDITPA apportionment should be construed in a manner to effectuate the presumption of fair taxation of a multistate corporation engaged in business

[15] As shown in the spreadsheet comparison contained on Department's closing brief, p. 25.

activities in the state). That is not to say the 30% exclusion method is a perfect apportionment method, but the case law does not demand perfection in apportionment, merely reasonableness. *See Moorman Mfg. Co.*, 437 U.S. 267, 272. *See also Container Corp.*, 463 U.S. 159, 192-93. Therefore, as the most reasonable of the offered alternatives, the Department should apply its 30% exclusion method to Taxpayer's 2015 CIT returns (subject to correction of the ratio transposed on the Department's worksheet Ex. AH, reduction of the Oil Insurance Limited's nonunitary dividends, and accurate calculation of payments already made or credited to Taxpayer's account).

Issue Six: Taxpayer is Entitled to Abatement of Penalty.

Although the hearing itself did not focus much on abatement of penalty, Taxpayer did argue in its protest letter that penalty in this case must be abated because, to the extent Taxpayer was liable for the assessment, it was based on a mistake of law made in good faith and on reasonable grounds pursuant to NMSA 1978, Section 7-1-69 (B). In its amended protest, Taxpayer further cited the *General Electric* decision and order, 2018 WL 1795457 (non-precedential), as support of its claim for abatement of penalty. Taxpayer also argued for abatement of penalty in its opening remarks at the hearing.

When a taxpayer fails to pay taxes due to the state because of negligence or disregard of rules and regulations, but without intent to evade or defeat a tax, NMSA 1978 Section 7-1-69 (2007) requires that

> there *shall* be added to the amount assessed a penalty in an amount equal to the greater of: (1) two percent per month or any fraction of a month from the date the tax was due multiplied by the amount of tax due but not paid, not to exceed twenty percent of the tax due but not paid.

(*italics* added for emphasis).

The statute's use of the word "shall" makes the imposition of penalty mandatory in all instances where a taxpayer's actions or inactions meet the legal definition of "negligence." *See Marbob Energy Corp. v. N.M. Oil Conservation Comm'n*, 2009-NMSC-013, ¶22, 146 N.M. 24 (use of the word "shall" in a statute indicates the provision is mandatory absent clear indication to the contrary). Regulation 3.1.11.10 NMAC defines negligence in three separate ways: (A) "failure to exercise that degree of ordinary business care and prudence which reasonable taxpayers would exercise under like circumstances;" (B) "inaction by taxpayer where action is required"; or (C) "inadvertence, indifference, thoughtlessness, carelessness, erroneous belief or inattention." By taking the inaction of not including the dividend income as business income, apportionable and subject to New Mexico corporate income tax, Taxpayer meets this definition of negligence, and thus is potentially subject to a civil negligence penalty under Section 7-9-69.

In instances where a taxpayer might otherwise fall under the definition of civil negligence generally subject to penalty, however, Section 7-1-69 (B) provides a limited exception: "[n]o penalty shall be assessed against a taxpayer if the failure to pay an amount of tax when due results from a mistake of law made in good faith and on reasonable grounds." A mistake of law is a "mistake about the legal effect of a known fact or situation," whereas a mistake of fact is a "mistake about a fact that is material to a transaction; any mistake other than a mistake of law." Black's Law Dictionary 1153-4 (10th ed. 2009). This agency has generally found that this good faith statutory exception to penalty generally requires some evidence that a taxpayer engaged in an informed consultation and decision-making process that the tax was not legally due. *Cf. C & D Trailer Sales v. Taxation and Revenue Dep't*, 1979-NMCA-151, ¶8-9, 93 N.M. 697 (penalty upheld where there was no evidence that the taxpayer "relied on any informed consultation" in deciding not to pay tax).

Although there was not much evidence presented that Taxpayer engaged in any informed consultation in this case, Mr. Sauer is an experienced C.P.A. who demonstrated expertise and familiarity in state income taxation throughout his testimony and in explaining why Taxpayer made the filing choices it did. Although ultimately incorrect, those explanations demonstrated reasonable and good faith mistakes about what the law required given the facts at play in this protest. The holdings of *Kraft* and *Conoco, Inc*. certainly create some reasonable basis for Taxpayer to believe its foreign dividend and Subpart F income were not apportionable to New Mexico, even if *NCR Corp.* and *Xerox* held to the contrary for combined return filers.

Moreover, the undersigned hearing officer abated penalty in the *General Electric* decision and order, a case that involved a similar substantive issue. *See General Electric*, 2018 WL 1795457 (non-precedential). To the extent that the *General Electric* decision and order might have clarified the issue further for Taxpayer, that decision was not issued until 2018, after Taxpayer had already made its mistake of law in this case. While it is a close analysis, the hearing officer finds that Taxpayer made a mistake of law in good-faith and on reasonable grounds pursuant to Section 7-1-69 (B). Therefore, assessed penalty should be abated in this matter.

Other Evidentiary Issues, Objections, and Arguments.

Original vs. Amended Return.

As a preliminary matter, the parties disagreed as to whether the original or amended return was the subject of the protest. The hearing officer ruled that the original return was the subject of the protest because the assessment had originated with the original return and because Taxpayer's protest letter referred to the original return rather than the amended return. *See* NMSA 1978, § 7-1-24 (B) (2019) (requiring a taxpayer to specify the grounds of the protest); *See also* NMSA 1978, §

7-1B-8 (D) (2019) (limiting protest to grounds stated in protest letter and answer). However, in the interest of administrative efficiency, the Department indicated on the record that it would apply the legal determinations made in this protest to the amended return (while still reserving each party's respective appeal rights).

Taxpayer's Invocation of Rule 615 and Rule 408

Taxpayer initially invoked the witness exclusion rule pursuant to Regulation 22.600.1.19 NMAC at the beginning of the hearing. Regulation 22.600.1.19 (E) NMAC reads that "[a]t the hearing, either party can invoke the exclusionary rule, excluding all witnesses other than the real party in interest, their representative, one main case agent, and any designated expert witness from the proceeding until the time of their testimony." The Department designated Protest Auditor Mary Griego as its case agent, as permitted under Regulation 22.600.1.19 NMAC. In addition to the case agent, the Department also asked that Mr. Armer be allowed to remain in the hearing as a necessary expert witness or alternatively under Rule 615 (C) of the New Mexico Rules of Evidence as an essential person to the presentation of the Department's case. Taxpayer objected to allowing Mr. Armer to remain in the room during the hearing.

The Department's argument is not persuasive for two reasons. First, the Department did not formally designate Mr. Armer in writing as an expert witness in a timely manner, as required under Regulation 22.600.1.19 (D) NMAC and therefore the witness exclusion rule remained applicable to Mr. Armer despite his obvious expertise in the subject of corporate income tax[16]. If the Department had timely designated its witness as an expert pursuant to that regulation, then the witness could have remained in the room throughout the proceeding under Regulation 22.600.1.19 (E). The

[16] There is no doubt of Mr. Armer's expertise in the area of corporate income tax from the Department's perspective. If the Department had timely designated him in writing as an expert witness, he almost certainly would have so qualified. But the act of formally designating someone as an expert witness is an important step in putting the opposing party on notice of the purpose of the witness.

Department's argument also was not persuasive because Rule 615 (C) has not been incorporated into the Administrative Hearings Office's hearing regulations addressing the witness exclusion rule and therefore is not directly controlling in this matter. *See* NMSA 1978, § 7-1B-6 (D) (1) (Formal Rules of Evidence do not apply).

Nevertheless, the Administrative Hearings Office looks to the Rules of Evidence for general guidance on the witness exclusionary rule. "The purpose of the rule excluding witnesses is to give the adverse party an opportunity to expose inconsistencies in the testimony and to prevent the possibility of one witness shaping his testimony to match that given by the other witnesses." *State v. Ortiz*, 1975-NMCA-112, ¶ 33, 88 N.M. 370 (internal quotes and citations omitted). Testimony regarding "simple objective facts" is "ordinarily not subject to tailoring, and if it were, it could have been exposed easily." *United States v. Prichard*, 781 F.2d 179, 183 (10th Cir. 1986). When looking specifically at the Rule 615 (C) exception, there is a six-part test to determine whether the exception applies and there is a presumption in favor of sequestration. *See United States v. Jackson*, 60 F.3d 128, 133 & 135 (2d Cir. 1995). *See also United States v. Deleon*, 2018 WL 1871418, at *2 (D.N.M. Apr. 17, 2018) (non-precedential but shows that a United States District Court Judge in the 10th Circuit has looked favorably on the 2nd Circuit's approach).

Looking to the primary purpose of the rule, reviewing the six factors, and using discretion in application of the exclusionary rule, the hearing officer allowed Mr. Armer to remain in the room except when there was testimony around the issue of business versus non-business income, an area on which Protest Auditor Mary Griego's testimony focused. Testimony proceeded in this manner for the first day of the hearing. This issue largely became moot on the second day of the hearing, when Taxpayer withdrew its invocation of the exclusionary rule except for instruction that Mr. Armer and Ms. Griego not discuss their testimony together during the course of the week.

Taxpayer also objected to the admission of certain exhibits it believed were protected as offers of settlement under Rule 408. Taxpayer eventually also withdrew its objection on this issue during the second day of the hearing before the hearing officer could make a formal ruling, rendering this issue moot.

Taxpayer Bill of Rights Argument and the Department's Counterargument.

Taxpayer in this case argued in its protest letter and in opening remarks that the Department violated the Taxpayer Bill of Rights by not clearly articulating the basis of its adjustments and assessments in this matter or not providing formal notice of an audit to Taxpayer. The Department counterargues that it was Taxpayer who forced its hand to act by failing to provide requested information, leaving the Department no choice but to issue its assessment with the information it could glean from Taxpayer's original 2015 corporate income tax return. In fact, one of the major themes of the Department's case throughout the proceeding and during closing argument was to emphasize what it perceived as a lack of cooperation from Taxpayer in responding to the Department's inquiries, requests for information, and other more formalized discovery requests such as interrogatories and requests for admissions.

NMSA 1978, Sections 7-1-4.1, 7-1-4.2, 7-1-4.3, and 7-1-4.4 (2003) constitute New Mexico's Taxpayer Bill of Rights (TABOR). New Mexico's TABOR does not include any specific, independent remedy for a violation of TABOR[17]. Instead, New Mexico's TABOR generally summarizes existing rights and obligations contained in the Tax Administration Act (TAA), NMSA 1978 Section 7-1-1 (1979). That does not mean that TABOR is unimportant or inoperative; only that it does not appear to be another source of independent relief beyond what is

[17] Compared to neighboring Colorado, which has an actionable constitutional amendment called a Taxpayer Bill of Rights where citizens can sue the State of Colorado for alleged violations. *See eg. Barber v. Ritter*, 196 P.3d 238 (Colo. 2008).

already articulated in the TAA statutory requirements. *See eg. Helmerich & Payne Int'l Drilling Co.*, 2019-NMCA-054, ¶¶ 12-13, 448 P.3d 1126, 1129–30 (while the Court of Appeals cited the broad provision of TABOR, it looked specifically to the underlying TAA statutory provision to outline the actionable parameters and potential remedies); *See eg. Breen v. State Taxation & Revenue Dept.*, 2012-NMCA-101, ¶¶ 26-28, 287 P.3d 379, 387–88 (again, the Court of Appeals looked to the underlying TAA statutory provision outlining the details of TABOR's confidentiality requirements). In other words, TABOR provides a consolidated general statement of specific statutory, controlling provisions contained elsewhere in the TAA. Similar to the Court of Appeals, the Administrative Hearings Office has looked to TABOR as a purpose statement to help ascertain and effectuate Legislative intent in interpreting the specific underlying statutory provisions of the TAA. *See In the Matter of the Protest of El Castillo Retirement Residences to Denial of Protest Issued Under Letter Id No. L1051055920 v. New Mexico Taxation and Revenue Department*, 2019 WL 3782593 (non-precedential; using TABOR to help interpret potentially competing TAA statutory provisions).

Ultimately, whether or not TABOR provides any independent mechanism for enforcement beyond the related TAA statutory provisions, TABOR is not determinative in this protest. The hearing officer certainly agrees that considering the magnitude of the adjustments the Department made in this case, in best practice the Department should have expounded further on reasons for the adjustments and its subsequent assessment to Taxpayer. Nevertheless, the hearing officer cannot say that the Department failed to meet the requirements of NMSA 1978, Section 7-1-4.2 (F) that a taxpayer be provided an explanation of the adjustments and the basis of the assessment in this matter. The Department in fact provided three brief explanations of its proposed adjustments in the March 21, 2017 Return Adjustment Notice: first, that that Taxpayer made an error on line 11 of the

Original CIT-1 return in calculating its New Mexico percent[age], a reference to the apportionment factor percentage; second, that Taxpayer made an error in allocating/apportioning income for determining taxable income rather than calculating the percentage on line 11 of the CIT-1 return; and third, Taxpayer erred by failing to attach Schedule CC to support line 12 of the CIT-1 return. [Taxpayer Ex. 6.2].

These three statements provided Taxpayer with a basic explanation for the adjustment, in that the Department disagreed with how Taxpayer allocated income and how Taxpayer apportioned the New Mexico percentage of taxable income, in addition to the absence of a required schedule to support the CIT-1 return. Additionally, the Return Adjustment Notice contained FYI-406, a statement explaining Taxpayer's rights in response to a notice of return adjustment, including a direction to contact the Department if Taxpayer disagreed with the adjustment. This additional FYI-406 also satisfies provisions of Section 7-1-4.2 (E) and Section 7-1-4.3 of TABOR. The assessment itself, which was based on the Return Adjustment Notice, complied with the requirements of NMSA 1978, Section 7-1-17 (2007) in that it was issued under the name of the Secretary and stated the nature and amount of assessed taxes.

Even before the Department issued either its Return Adjustment Notice or Notice of Assessment, it sought additional information from Taxpayer related to the Original CIT-1 return to process the claim for refund on that return. On February 13, 2017, the Department sent Taxpayer a letter request for additional information to the very same address Taxpayer listed on the 2015 CIT-1 return. [Dept. Ex. AH]. If the Department did not use best practice in the subsequent return adjustment notice, in fairness it must also be said that Taxpayer also did not follow best practice itself in failing to provide requested substantiation for its own substantial $19,422,282.00 refund claim. As the Department argues, at some level Taxpayer bears responsibility to provide requested, accurate records to support its return. When Taxpayer failed to provide the Department with the requested records needed to verify the 2015 CIT-1 return, under NMSA 1978, Section 7-1-11 (E) (2019), the Department was permitted to use other reasonable methods to determine Taxpayer's corporate income tax liability, which it obviously did in this case in the form of the return adjustment notice and subsequent assessment. While the subsequent protest and hearing process revealed that the Department's adjustment contained distortion in need of correction, the Department's actions at the time were reasonable considering the information it had available to it and the lack of response from Taxpayer about the additional documentation the Department sought.

Conclusion

Both sides in this protest did an excellent and commendable job in presenting their respective positions in this complex, corporate income tax protest. With exception of elimination of the Oil Insurance Limited nonunitary dividends from apportionment, removal of the assessed penalty, and application of the Department's 30% exclusion method as an alternative apportionment method against Taxpayer's remaining 2015 apportionable income, Taxpayer's protest **IS DENIED**.

CONCLUSIONS OF LAW

A. Taxpayer filed a timely, written protest of the Department's assessment and jurisdiction lies over the parties and the subject matter of this protest.

B. This protest was limited to Taxpayer's original 2015 CIT-1 return, but the Department agreed to apply the legal determinations (subject to the right of appeal) made in this protest against Taxpayer's amended 2015 return. *See* NMSA 1978, § 7-1-24 (B) (2019); s*ee also* NMSA 1978, § 7-1B-8 (D) (2019).

C. The hearing was timely set within 90-days of protest under Section 7-1B-8.

D. Delay in issuing a decision in a complex tax protest does not invalidate the jurisdiction of a hearing officer to make a ruling in a tax matter. *See KPI*, 2006-NMCA-026, ¶55, 139 N.M. 177, 192, *rev'd on other grounds and certiorari as to corporate income tax issues quashed, Kmart Corp. v. Taxation & Revenue Dep't.*, 2006-NMSC-006, 139 N.M. 172; *see also Ranchers-Tufco Limestone v. Revenue*, 1983-NMCA-126, ¶13 (delay in action is not a defense to enforcement in a tax action).

E. Under NMSA 1978, Section 7-1-17 (C) (2007), the assessment issued in this case is presumed correct. Consequently, Taxpayer has the burden to overcome the assessment. *See Archuleta*, 1972-NMCA-165, ¶11, 84 N.M. 428. *See also Casias Trucking*, 2014-NMCA-099, ¶8.

F. Taxpayer rebutted the presumption of correctness as to the original assessed amount of corporate income tax due. *See MPC Ltd.*, 2003-NMCA-21, ¶13, 133 N.M. 217.

G. Taxpayer maintained the burden of establishing by clear and cogent evidence that the state seeks to tax extraterritorial value. *See Allied-Signal, Inc.*, 504 U.S. 768, 782, (citing *Exxon Corp*., 447 U.S. 207, 224).

H. Taxpayer, as an out of state corporation engaged in the transaction of business into and from New Mexico, was subject to New Mexico's corporate income tax under Section 7-2A-3.

I. Under principals of statutory construction, and in order to effectuate all terms of the statute consistent with other provisions of the statute and the applicable general body of law, NMSA 1978, Section 7-2A-2 (Q) (2014) should be read broadly as adopting the well-understood and developed "three unities" test articulated in Supreme Court jurisprudence on unitary businesses. By meeting the three statutory conditions of Section 7-2A-2 (Q), a foreign corporation affiliated with another corporation engaged in New Mexico business activity has itself necessarily engaged in unitary business activities within New Mexico and the United States. *See N.M. Indus. Energy Consumers*, 2007-NMSC-053, ¶ 20, 142 N.M. 533. *See also Helman*, 1994-NMSC-023, ¶23, 117 N.M. 346. *See also Hayes*, 1963-NMSC-095, ¶9, 75 N.M. 70.

J. Because Taxpayer held less than a 5% stake in Oil Insurance Limited, Oil Insurance Limited and Taxpayer did not meet the statutory definition of unitary corporations under Section 7-2A-2 (Q).

K. Under the "three unities" unitary business test contained in case law and under Section 7-2A-2 (Q), Taxpayer was unitary with the remaining fourteen foreign subsidiaries because of a clear flow of value between Taxpayer and the foreign subsidiaries facilitated by functional integration, centralization of management, and economies of scale. *See Mobil Oil Corp.*, 445 U.S. 425, 435; *See also Container Corp.*, 463 U.S. 159, 178, 103 S. Ct. 2933, 2947, 77 L. Ed. 2d 545 (1983); *MeadWestvaco Corp.*, 553 U.S. 16, 19 (2008); *Allied-Signal, Inc.*, 504 U.S. at 772; *Hunt Wesson*, 528 U.S. at 460; *Exxon Corp.*, 447 U.S. 207, 224 (1980); *NCR Corp.*, 1993-NMCA-060, ¶ 15, 115 N.M. 612, 616.

L. Taxpayer's unitary foreign dividend income and Subpart F income constituted business income pursuant to the dispositional and functional test of Section 7-4-2 (A), making that income apportionable to New Mexico for state corporate income tax purposes. *See NCR Corp.*, 1993-NMCA-060, ¶¶ 26-34.

M. Taxpayer's check-the-box income, required to be reported as federal income under 26 C.F.R. § 301.7701-3, is business income under the dispositional test of Section 7-4-2 (A) and subject to New Mexico apportionment. *See NCR Corp.*, 1993-NMCA-060, ¶¶ 28-34; *see also* §7-2A-2 (C) (defining New Mexico base income as federal taxable income as calculated under the I.R.C.); *see also* Department Regulation 3.5.1.9 (A) NMAC.

N. The holding of *Conoco, Inc.*, 1997-NMSC-005, only expressly rejected New Mexico's statutory treatment of foreign dividend income for separate entity filers and has not been extended to combined return filers.

O. New Mexico's corporate income tax scheme, vis-à-vis the unitary combined filer reporting method, does not violate the Foreign Commerce Clause because it is a tax on the income of a unitary corporation doing business in New Mexico rather than a direct tax on a foreign corporation. *See NCR Corp.*, 1993-NMCA-060; *See also Xerox*, 2003 WL 24889474, (non-precedential)*; Morton Thiokol, Inc.*, 254 Kan. 23, 864 P.2d 1175 (Kan. 1993); *Du Pont*, 675 A.2d 82, (Me. 1996).

P. Unlike the facts and circumstances in *Japan Line*, 441 U.S. 434, New Mexico's imposition of tax in this case is not against a foreign corporation, but against the apportioned share of the income of a unitary corporation doing business in New Mexico, making this case distinguishable from *Japan Line*. This case is also distinguishable from *Japan Line* in that *Japan Line* involved a property tax assessment, where situs is an important consideration, versus the apportioned income tax of a unitary business, where situs is not as important. *See Container Corp.*, 463 U.S. 159 (1983).

Q. There is no equal protection violation for distinguishment in treatment between unitary businesses filing a combined return and single-entity filers because the unitary business principal provides a rational justification for the Legislature's disparate treatment. *See Anaconda Co.*, 1979-NMCA-158, ¶¶ 22-23, 94 N.M. 202, 210,; *See also Michael J. Maloof & Co*, 80 N.M. 485 (1969); *See also Madden*, 309 U.S. 83, 87-88 (1940); S*ee also Pinghua Zhao*, 2014-NMSC-025, ¶19.

R. Taxpayer overcame the presumption of correctness as to the dollar amount of the original assessment, which was premised on the standard three-factor apportionment formula. The Department's main corporate income tax witness also conceded that the standard three-factor apportionment formula in this case resulted in obvious distortion, meaning that the Department did not reestablish correctness of the original, assessed amount. *See MPC Ltd.*, 2003-NMCA-21, ¶13, 133 N.M. 217.

S. Because of the obvious distortion present in the standard, three-factor apportionment formula, Taxpayer was entitled to a reasonable, alternative apportionment method under Section 7-4-19. *See Hans Rees Sons, Inc.*, 283 U.S. 123, 135 (1931); S*ee also Norfolk & W. R. Co.*, 390 U.S. 317, 329 (1968); *Jefferson Lines*, 514 U.S. 175, 185 (1995); *Goldberg*, 488 U.S. 252, 264-65 (1989); *Whirlpool Props., Inc.*, 208 N.J. 141, 165, 26 A3D 446 (2011); *KPI*, 2006-NMCA-026, ¶ 50-51, 139 N.M. 177; *Twentieth Century-Fox Film Corp.*, 299 Or. 220, 233, 700 P.2d 1035 (1985).

T. Taxpayer did not establish the reasonableness of either of its proffered alternative apportionment methods, and thus failed to carry its burden to establish the reasonableness of the alternative apportionment method. *See Twentieth Century-Fox Film Corp.*, 299 Or. 220, 233, 700 P.2d 1035, 1044.

U. The Department's 30% exclusion alternative apportioned method is the most reasonable alternative method offered by either party. This method addresses both the underlying, obvious distortion from multiyear accumulated foreign dividends under the original assessment while still recognizing the economic reality that Taxpayer's New Mexico operations in the Permian Basin played an important role in furthering Taxpayer's unitary oil and gas business. *See KPI*, 2006-NMCA-026, ¶51; *see also Pub. Serv. Co. of N.M.*, 2007-NMCA-050, ¶ 33.

V. Under NMSA 1978, Section 7-1-67 (2007), Taxpayer is liable for accrued interest under the assessment. Interest continues to accrue until the tax principal is satisfied.

W. Taxpayer established that it made a mistake of law, in good faith and on reasonable grounds, and thus is not subject to a civil negligence penalty under NMSA 1978, Section 7-1-69 (B).

X. The Department's Return Adjustment Notice and Original Assessment met the minimum requirements articulated in the Taxpayer Bill of Rights, as specifically detailed by the related statutory provisions of the Tax Administration Act.

For the foregoing reasons, the Taxpayer's protest **IS PARTIALLY GRANTED AND PARTIALLY DENIED**. **IT IS ORDERED** that the Department recalculate the assessment by using the Department's 30% exclusion alternative apportionment method against Taxpayer's 2015 unitary income, including the foreign sourced dividend, Subpart F, and check-the-box income but excluding the dividend income generated by non-unitary Oil Insurance Limited. **IT IS FURTHER ORDERED** that penalty is abated. **IT IS FINALLY ORDERED** that Taxpayer pay the recalculated, outstanding 2015 corporate income tax and interest.

DATED: August 24, 2021.

Brian VanDenzen
Chief Hearing Officer
Administrative Hearings Office
P.O. Box 6400
Santa Fe, NM 87502

NOTICE OF RIGHT TO APPEAL

Pursuant to NMSA 1978, Section 7-1-25 (2015), the parties have the right to appeal this decision by *filing a notice of appeal with the New Mexico Court of Appeals* within 30 days of the date shown above. If an appeal is not timely filed with the Court of Appeals within 30 days, this Decision and Order will become final. Rule of Appellate Procedure 12-601 NMRA articulates the requirements of perfecting an appeal of an administrative decision with the Court of Appeals. Either party filing an appeal shall file a courtesy copy of the appeal with the Administrative Hearings Office contemporaneous with the Court of Appeals filing so that the Administrative Hearings Office may begin preparing the record proper. The parties will each be provided with a copy of the record proper at the time of the filing of the record proper with the Court of Appeals, which occurs within 14 days of the Administrative Hearings Office receipt of the docketing statement from the appealing party. *See* Rule 12-209 NMRA.

CERTIFICATE OF SERVICE

On August 24, 2021, a copy of the foregoing Decision and Order was submitted to the parties listed below in the following manner:

VIA Email Only *VIA Email Only*

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____

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