BEFORE THE HEARING OFFICER
OF THE TAXATION AND REVENUE DEPARTMENT
OF THE STATE OF NEW MEXICO

IN THE MATTER OF THE PROTEST OF
PRODUCTION CREDIT ASSOCIATION
OF EASTERN NEW MEXICO NO. 98-58
ID. NO. 01-508114-001, PROTEST TO
DENIAL OF CLAIMS FOR REFUND OF
CORPORATE INCOME TAXES FOR
TAX YEARS 1992,1993,1994,1995 AND 1996.

DECISION AND ORDER

This matter comes on for determination before Gerald B. Richardson, Hearing Officer, based upon a stipulation of facts, stipulated exhibits and briefs of the parties. Production Credit Association of Eastern New Mexico, hereinafter, "PCA", was represented by Curtis W. Schwartz, Esq., of Modrall, Sperling, Roehl, Harris & Sisk, P.A. The Taxation and Revenue Department, hereinafter, "Department", was represented by Frank D. Katz, Chief Counsel. Based upon the evidence and the arguments presented, IT IS DECIDED AND ORDERED AS FOLLOWS:

FINDINGS OF FACT

1. PCA timely filed New Mexico corporate income tax returns and timely paid New Mexico corporate income taxes for the tax years 1992, 1993, 1994, 1995 and 1996.

2. On April 23, 1996, PCA submitted a claim for refund of all New Mexico income tax paid for its 1992 tax year in the amount of $56,745.

3. On September 9, 1997, PCA submitted claims for refund of all New Mexico income taxes paid for the tax years 1993, 1994, 1995, and 1996 in the total amount of $287,037.

4. PCA based its claims for refund for tax years 1992-1996 upon its understanding that, as a matter of law, it is a federal instrumentality immune or exempt from state income taxation pursuant to the Supremacy Clause of the United States Constitution.

5. The Department did not act on PCA's claim for refund for its 1992 tax year within the 120-day time period provided for by § 7-1-26 NMSA 1978, rendering the claim for refund deemed denied.

6. On September 18, 1996, PCA timely filed a protest to the Department's deemed denial of its claim for refund for its 1992 tax year.

7. On January 26, 1998, in a letter from Mike D. Baca, Supervisor, Corporate Income Tax Unit, to PCA, the Department denied PCA's claims for refund for its 1993 through 1996 tax years.

8. On April 23, 1998, PCA timely filed a protest to the department's denial of its claims for refund for its 1993-1996 tax years.

9. In this consolidated protest proceeding, PCA seeks all amounts claimed as refunds for its 1992-1996 tax years, plus interest thereon, as provided in § 7-1-68 NMSA 1978.

10. PCA is a component of the federal Farm Credit System.

11. The Farm Credit System is a network of farmer and rancher-owned cooperative lending institutions.

12. The lending and financial activities of PCA are under the direct supervision and approval of, and subject to standards prescribed by, the Farm Credit Bank of Texas and, ultimately, the federal Farm Credit Administration.

13. Production credit associations were initially capitalized and owned entirely by the United States, though Congress hoped that production credit association earnings could be used to retire its stock.

14. Congress hoped that as the production credit associations retired government held stock, that they could become local lenders, owned by borrowers.

15. Congress' hope was realized by the 1960's, by which time the production credit associations were owned entirely by borrowers with the United States not having any ownership interest.

16. The Production Credit Association of Eastern New Mexico (PCA) has its principal place of business in Clovis, New Mexico.

17. PCA is a federally chartered corporation incorporated pursuant to the provisions of the Farm Credit Act of 1933.

18. PCA was incorporated pursuant to federal law utilizing a Farm Credit Administration pre-printed set of Articles of Incorporation dated February 15, 1934.

19. PCA was duly chartered on February 27, 1934 as an agricultural credit cooperative pursuant to the provisions of the Farm Credit Act of 1933.

20. The charter was issued by the Farm Credit Administration.

21. Pursuant to federal statute, PCA is a federal instrumentality. 12 U.S.C. §§ 2071(a), 2071 (b)(7), 2077. *See also,* 12 U.S.C. § 2279c(b).

22. The United States Farm Credit Administration chartered PCA in 1934 under its original name, the "Clovis Production Credit Association."

23. PCA subsequently changed its name to the current one, effective March 1, 1984.

24. The corporate purpose for PCA was and is to exercise powers granted to it by Congress under the Farm Credit Act of 1933 as it existed or may be amended.

25. Pursuant to a "Certificate of District To Be Served" issued by the Farm Credit Administration, the Farm Credit Administration limited PCA to lending in Quay, Curry, DeBaca, Guadalupe and Roosevelt Counties in New Mexico.

26. PCA loans money for periods of ten years or less.

27. PCA does not lend to the general public, but only to qualified ranchers or farmers.

28. PCA is not a depository bank and has no deposit insurance.

29. Pursuant to bylaws imposed by the Farm Credit Administration, PCA is authorized to issue Class A and Class B stock with a par value of five dollars.

30. Though its bylaws authorize PCA to offer other classes of common and preferred stock at $5 par value, it has never done so.

31. All PCA borrowers as a requirement of obtaining a loan are required to purchase Class B $5 par voting stock of PCA in an amount equal to 10% of the unpaid principal balance of the loan.

32. As part of the loan, sufficient proceeds are generally advanced to purchase the required Class B Stock.

33. Class B stock is not entitled to dividends.

34. Each holder of Class B voting stock has only one vote in PCA affairs, regardless of the number of shares held. In the case of a joint loan, only one of the joint borrowers may vote, as authorized by the other joint borrowers.

35. Class B stock may be retired at the lesser of par or book value as the loan is paid down, as long as the borrower maintains the prescribed stock-to-loan balance ratio.

36. Alternatively, Class B stock may be converted to non-voting Class A stock also with a par value of five dollars.

37. Class A stock may be retired for the lesser of par or book value.

38. Class A stock is not entitled to dividends.

39. PCA obtains its funds from the Farm Credit Bank of Texas; though until March 1991, it obtained funds from the Farm Credit Bank of Wichita.

DISCUSSION

This case presents the issue of whether New Mexico is permitted under the Supremacy Clause of the United States Constitution to impose income tax upon the income of the Production Credit Association of Eastern New Mexico, hereinafter, "PCA." It is undisputed that PCA, as a production credit association of the federal Farm Credit System, is a federal instrumentality. *See,* 12 U.S.C. §§ 2071(a), 2071(b)(7), 2077 and 2279d(b). PCA argues that its status as a federal instrumentality stands as an absolute bar to state taxation and that no further inquiry is either necessary or proper. The Department argues that not every federal instrumentality is immune from tax, that Congress explicitly waived the exemption from state taxation of production credit associations when the Federal Government no longer owned stock in them, and that even though the language waiving the exemption from state tax was dropped in later amendments of the Farm Credit Act, application of principles of statutory construction leads to the conclusion that Congress did not intend to confer tax immunity upon production credit associations by those amendments.

The Intergovernmental Tax Immunity Doctrine

The immunity of the Federal Government and its instrumentalities from state taxation was first announced in ***McCulloch v. Maryland,*** 17 U.S. (4 Wheat.) 316 (1819). In that case, Chief Justice Marshall ruled that the Supremacy Clause prevented Maryland from levying a stamp tax on bank notes issued by the Baltimore branch of the Bank of the United States, a corporation chartered by Congress. This decision contains the now famous dictum by the Court, "[T]hat the power to tax involves the power to destroy;...", ***Id.*** at 431. The Court, recognizing the sovereign power of the states to tax, sought to reconcile the states' taxing power with the recognition in the Constitution that the Constitution is the supreme law of the land. It concluded:

> If the controlling power of the states be established; if their supremacy as to taxation be acknowledged; what is to restrain their exercising control in any shape they may please to give it? Their sovereignty is not confined to taxation; that is not the only mode in which it might be displayed. The question is, in truth, a question of supremacy; and if the right of the states to tax the means employed by the general government be conceded, the declaration that the constitution, and the laws made in pursuance thereof, shall be the supreme law of the land, is empty and unmeaning declamation.

17 U.S. at 431. It thus struck down Maryland's tax because it interfered with the federal banking function established by Congress. The Court also recognized that ultimately, the power to determine the extent of immunity from state taxation and regulation rests with Congress, which is best situated to determine whether a state tax interferes with a federal function, stating:

> In the legislature of the Union, alone, are all represented. The legislature of the Union alone, therefore, can be trusted by the people with the power of controlling measures which concern all, in the confidence that it will not be abused.

17 U.S. at 431. Accordingly, since ***McCulloch***, the rule with respect to taxation of federal instrumentalities has been that if Congress does not authorize state taxation or regulation, the possibility of interference with substantive federal policy is sufficient to raise a presumption of

immunity. ***See, Osborn v. Bank of U.S.***, 22 U.S. (9 Wheat.) 738, 865 (1824) which rejected the argument that when Congress is silent, the presumption is in favor of a state's ability to impose a tax on a federal instrumentality.

As the law of intergovernmental tax immunity developed, immunity from state taxation was accorded by the Federal Courts not only to the Federal Government and its instrumentalities, but also to persons dealing with the Federal Government, because the cost of the tax would ultimately be passed on to the Federal Government. ***See, Panhandle Oil Co. v. Mississippi ex rel. Knox,*** 277 U.S. 218 (1928). Beginning with ***James v. Dravo Contracting Co.***, 302 U.S. 134 (1937), which upheld the imposition of a state tax on a federal contractor building locks and dams, however, the modern trend, with respect to federal contractors, has been to uphold a state tax if it is non-discriminatory and where the legal incidence of the tax is on the private party and not on the Federal Government or agency. ***See,*** also, ***U.S. v. New Mexico,*** 455 U.S. 720 (1982).

There has also been litigation over what constitutes a federal instrumentality entitled to state tax immunity. Thus, it has been held that instrumentalities do not include independent contractors, employees or others dealing for their own purposes with the Federal Government, but only those entities, "so assimilated by the government as to become one of its constituent parts." ***U.S. v. Township of Muskegon,*** 355 U.S. 484, 486 (1958). In this case, because production credit associations are statutorily designated instrumentalities of the Federal Government, their status as an instrumentality is not in dispute. Because of the rather unique history of congressional enactments addressing their taxability, however, their immunity from taxation is hotly contested by the parties.

The Farm Credit Systems and Production Credit Associations

The Farm Credit System is a nationwide network of farmer and rancher owned cooperative lending institutions designed to serve the credit needs of the agricultural sector. The system began in 1916 with the enactment of the Federal Farm Loan Act which authorized the creation of twelve regional federal land banks. Pub. L. No. 64-158, § 4 (1916). Federal land banks could only make loans secured by first mortgages on farm and ranch property. Pub. L. No. 64-158, § 12. In 1923, Congress created federal intermediate credit banks to make other types of agricultural loans which were not secured by mortgages on farm lands. In 1988, federal land banks and federal intermediate credit banks were merged into farm credit banks. Pub. L. No. 100-233, Title IV, § 410 (1988).

Production credit associations were created by Congress in the Farm Credit Act of 1933 to provide short to intermediate term loans to ranchers and farmers. Pub. L. No. 73-98, § 20 (1933). Production credit associations were created during the Great Depression in response to the failure of commercial banks to provide adequate and affordable credit to farmers and the inefficiencies, costs and inflexibility of centralized government lending programs. S. Rep. No. 124, 73rd Congress, 1st Session, at 2 (1933). As stated in the Senate Committee on Banking and Currency Report on the legislation:

> The policy of this bill is to provide the stimulus in the form of Government capital and supervision to the establishment of local institutions in which farmers are participants and owners and through which necessary credit may be provided on a safe business basis and at reasonable cost.

S. Rep. No. 124, 73rd Cong., 1st Sess at 2 (1933). Production credit associations were initially capitalized and owned entirely by the Federal Government, but Congress hoped that earnings of the associations could be used to retire stock held by the Government so that they would eventually be owned entirely by their own members and borrowers. ***Id.*** In fact, by 1968, all

production credit associations were owned entirely by their borrower-members. ***See,*** H.R. Rep. No. 593, 92nd Cong., 1st Sess. (1971), ***reprinted in*** 1971 U.S.C.C A.N. 2091, 2098. At their creation, production credit associations were organized, chartered and regulated by the Governor of the Farm Credit Administration. Pub. L. No. 73-98, § 20. They remain subject to the regulation of the Farm Credit Administration, an independent agency of the Executive Branch of the Federal Government responsible for the regulation and examination of entities within the Farm Credit System. ***See,*** 12 U.S.C. §§ 2252 and 2241. The Farm Credit System and the Farm Credit Administration were reorganized by Congress by the Farm Credit Amendments Act of 1985, Pub.L. 99-205. One of the purposes of these amendments was to lessen the Government's day-to-day control of the Farm Credit System.

> The Farm Credit Administration would abandon past practices that amounted to day-to-day participation in management of the System activities and would become an arm's length regulator like other similar federal agencies....Stronger federal oversight and regulation of the System will result in cutting the principal organizational ties between the Farm Credit Administration, the regulator, and the Farm Credit System banks and associations.

H.R. Rep. No. 425 at 3,12, 1985 U.S.C.C.A.N. at 2589, 2598. These changes recognized that the banks and associations, including production credit associations, were no longer owned by the Federal Government. Thus, they were to be treated as independent, but regulated entities. The governing structure of the Farm Credit Administration was also modified. The Farm Credit Administration had been directed by a part time board that chose a full-time governor to run the agency. The 1985 Act, however, shifted the management of the Farm Credit Administration to a full time, three member presidentially appointed board, which became more of an arm's length regulator of the Farm Credit System institutions, and references to the Governor of the Farm

Credit Administration were removed from the laws concerning production credit associations. ***See,*** H.R. Rep. No. 425 at 3 and 28, 1985 U.S.C.C.A.N.at 2589 and 2616.

The Legislative History of the Taxability of Production Credit Associations

Commencing with the legislation creating production credit associations in 1933, Congress chose to expressly provide guidance with respect to the extent to which the associations, and their property and obligations would be taxable. Specifically, it chose to limit the immunity from taxation which would otherwise be accorded a federal instrumentality, providing as follows:

> The Central Bank for Cooperatives, the Production Credit Corporations, *Production Credit Associations,* and Banks for Cooperatives, organized under this Act, and their obligations, shall be deemed to be instrumentalities of the United States, and as such, any and all notes, debentures, bonds and other such obligations issued by such banks, *associations*, or corporations shall be exempt both as to principal and interest from all taxation (except surtaxes, estate, inheritance and gift taxes) now or hereafter imposed by the United States or by any State, Territorial, or local taxing authority. *Such banks, associations or corporations, their property, their franchises, capital, reserves, surplus and other funds, and their income shall be exempt from all taxation now or hereafter imposed by the United States or by any State, Territorial or local taxing authority; except that any real property and any tangible personal property and any tangible property of such banks associations and corporations shall be subject to Federal, State, Territorial, and local taxation to the same extent as other similar property is taxed. The exemption provided herein shall not apply with respect to any Production Credit Association or its property or income after the stock held in it by the Production Credit Corporation has been retired,* or any Production Credit Corporation or Bank for Cooperatives, or its property or income after the stock held in it by the United States has been retired.

Pub. L. No. 73-98, § 63, 48 Stat. at 267 (emphasis added). Thus, from the outset of their creation, the exemption from state income taxation accorded to production credit associations was expressly stated and expressly limited to periods in which some portion of the stock of an

association was owned by the Production Credit Corporation, a federally chartered and owned corporation created by the same Farm Credit Act of 1933 to capitalize production credit associations.

Although Congress made a number of changes in the Farm Credit System in the Farm Credit Act of 1971, and although there were no production credit associations entitled to income tax immunity, because all such associations were now owned entirely by their members, the provisions were retained which limited the income tax immunity of production credit associations to those which still had some portion of their stock owned by the Governor of the Farm Credit Administration. As amended by the 1971 Act, these provisions read as follows:

> Each production credit association and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by such associations shall be exempt, both as to principal and interest from all taxation (except surtaxes, estate, inherintance and gift taxes) now and hereafter imposed by the United States, any state, territorial or local taxing authority. *Such associations, their property, their franchises, capital reserves, surplus, and other funds and their income shall be exempt from all taxation now and hereafter imposed by the United States and any State, territorial or local taxing authority; except that interest on the obligations of such associations shall be subject only to federal income tax in the hands of the holder thereof pursuant to the Public Debt Act of 1941 (31 U.S.C. 742(a)) and except that any real and personal property of such associations shall be subject to federal, State, territorial and local taxation to the same extent as similar property is taxed. The exemption provided in the preceding sentence shall apply only for any year or part thereof in which stock in the production credit association is held by the Governor of the Farm Credit Administration.*

Farm Credit Act of 1971, Title II, § 2.17, complied at 12 U.S.C. § 2077 (emphasis added).

In 1985, as part of the amendments enacted by the Farm Credit Amendments Act of 1985, the last two sentences of 12 U.S.C. § 2098, which are italicized in the quotation directly above,

were removed from the statute. Pub. L. 99-205, Title II, § 205(e)(16), 99 Stat. 1678, 1705 (1985). Thus, the language providing for income tax exemption and the language qualifying the income tax exemption to instances where the the stock in a production credit association is held by the Governor of the Farm Credit Administration was removed.

There is nothing in the legislative history of the 1985 amendments to indicate that Congress, by removing the language concerning the limited immunity of production credit associations from taxes on their income, property, funds and reserves, intended to confer broad and unlimited tax immunity on such associations, beyond the immunity for their notes, debentures and other obligations conferred by the first sentence of 12 U.S.C. § 2077. Rather, with reference to Section 205, which contained these amendments, the House Report states:

> [Section 205] contains numerous technical and conforming amendments to the provisions of the Farm Credit Act of 1971 affected by changes in the basic powers, duties and authorities of the Farm Credit Administration. This section would amend the appropriate provisions of the Act to delete the requirement for specific approvals by the Farm Credit Administration of certain activities of the banks and associations by deleting the general authority of the Farm Credit Administration to supervise System institutions. These changes are consistent with one of the major purposes of the legislation which is to establish the Farm Credit Administration as an arms length regulator of the system institutions and to take it out of certain activities of the System which would involve it in management discretion of such institutions.

H.R. Rep. No. 425 at 28, 1985 U.S.C.C.A.N. at 2615. Thus, the amendments are described as technical and conforming amendments, intended to be consistent with the purpose of the 1985 Amendments Act to change the management function of the Farm Credit Administration to being a regulator rather than day-to-day manager of production credit associations. There is no mention of any tax implications whatsoever.

Are Production Credit Associations exempt from income taxation by virtue of their status as a federal instrumentality?

The issue of the state tax immunity of production credit associations first arose after the 1985 amendments to the Farm Credit Act. Four production credit associations in Arkansas brought suit in the United States District Court of the Eastern District of Arkansas seeking declaratory judgment and injunction that they were exempt from Arkansas sales and income taxation. The District Court granted summary judgment on behalf of the production credit associations based upon their status as federal instrumentalities whose immunity from state taxation was not expressly waived by Congress. Arkansas appealed, raising the same arguments the Department raises herein. The Court of Appeals affirmed by a divided panel. ***Farm Credit Services of Central Arkansas, PCA v. State of Arkansas,*** 76 F.3d 961 (8th Cir. 1996). The majority opinion concluded, as did the District Court below, that because the federal statutes no longer contained an express waiver of the Production Credit Associations' implied immunity as federal instrumentalities, they were immune from Arkansas taxes. ***Id.,*** at 964. Judge Loken wrote a dissenting opinion, stating that Congress was best qualified to balance the competing interests involved in applying the doctrine of intergovernmental immunity to federal instrumentalities and that the application of normal rules of statutory construction could lead only to the conclusion that the 1985 technical amendments were not intended to confer an implied constitutional immunity from tax. ***Id.,*** at 965-967.

The Supreme Court granted certiorari and reversed the Court of Appeals. ***Arkansas v. Farm Credit Services of Central Arkansas,*** __ U.S. ___, 117 S.Ct. 1776 (1997). It did not reach the issue of whether production credit associations were immune from state tax under the Supremacy Clause. Rather, it held that the Federal District Court lacked subject matter

jurisdiction to determine the issue of immunity from state tax because of the operation of the Tax Injunction Act, 28 U.S.C. § 1341, which provides:

> The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State.

The Court recognized that the Tax Injunction Act was a congressional statement with respect to the balance of powers between the States and the Federal Government that federal courts should not interfere with the ability of the States to define and elaborate their own laws and administrative processes, especially in an area as important as taxation, which is a power held concurrently by the States and the Federal Government. ***Id.,*** 117 S.Ct. at 1779-1780. Although the only exception to the jurisdictional bar contained in the Tax Injunction Act is where a plain, speedy and efficient remedy is not available from the state courts, the Court has recognized that under our constitutional system, the Federal Government has sovereign interests which it must be allowed to protect. Thus, the Court has also recognized an exception to the jurisdictional bar of the Tax Injunction Act when the United States sues to protect itself or its instrumentalities from state taxation. ***Department of Employment v. United States,*** 385 U.S. 355, 358 (1966). In the ***Department of Employment*** case, however, the United States was a co-plaintiff with the federal instrumentality, the Red Cross, in challenging the imposition of a state tax. In the litigation involving the four Arkansas production credit associations, they sued on their own. Thus, the issue before the Supreme Court in the ***Arkansas v. Farm Credit Services*** case was whether federal instrumentalities fall under the exception to the Tax Injunction Act when they sue without the United States as co-plaintiff. In concluding that the federal instrumentality status of production credit associations is not sufficient for them to escape the prohibition of the Tax

Injunction Act, the Court distinguished production credit associations from the United States or its agencies, such as the National Labor Relations Board, stating:

> Whatever may be the rule under the Tax Injunction Act where a federal agency or body with substantial regulatory authority brings suit, PCA's [Production Credit Associations] are not entities of that description. PCA's are not granted the right to exercise government regulatory authority but rather serve specific commercial and economic purposes long associated with various corporations chartered by the United States.
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> The PCA's' business is making commercial loans, and all their stock is owned by private entities. Their interests are not coterminous with those of the Government any more than most commercial interests. Despite their formal and undoubted designation as instrumentalities of the United States, and despite their entitlement to those tax immunities accorded by the explicit statutory mandate, PCA's do not have or exercise power analogous to that of the NLRB [National Labor Relations Board] or any of the departments or regulatory agencies of the United States. This sufficies for us to conclude that instrumentality status does not in and of itself entitle an entity to the same exemption the United States has under the Tax Injunction Act.

Id., 117 S.Ct. at 1782.

After the Supreme Court reversed the lower court determinations that the Arkansas associations were immune from Arkansas income and sales taxes, suit was brought in the Chancery Court of Pulaski County, Arkansas by the same production credit associations to determine the issue of tax immunity. On July 1, 1998, the Chancery Court granted summary judgment to the associations. The Chancery Court ruled on the same basis as the majority of the Eighth Circuit Court of Appeals panel, that in the absence of an express congressional waiver of immunity, production credit associations are immune from Arkansas' taxes based upon their federal instrumentality status. The decision is unreported but is contained in the record herein.

Farm Credit Services of Central Arkansas, PCA, et al. v. State of Arkansas, Chancery Court of Pulaski County Arkansas, No. 94-4931.

The Department draws from the language of the Court in ***Arkansas v. Farm Credit Services of Central Arkansas,*** quoted on page 16, herein, which strongly distinguished the activities and powers of production credit associations from those of the Federal Government, to argue that the federal instrumentality status of production credit associations, in and of itself, should not immunize them from state income taxation. In support, the Department cites to the following language from the Supreme Court's opinion in ***United States v. New Mexico***, 455 U.S. 720 (1982):

> What the Court's cases leave room for, then, is the conclusion that tax immunity is appropriate in only one circumstance: when the levy falls on the United States itself, *or on an agency or instrumentality so closely connected to the Government that the two cannot realistically be viewed as separate entities, at least insofar as the activity being taxed is concerned.*

455 U.S. at 735, 102 S.Ct at 1383 (emphasis added). The Department thus argues that the result in the ***Arkansas Farm Credit Services*** case, which effectively held that all federal instrumentalities are not so closely aligned with the Federal Government to support granting them the same exemption from the jurisdictional bar of the Tax Injunction Act, and the language from ***U.S. v. New Mexico*** which appears to limit the tax immunity under the Supremacy Clause to instrumentalities which are closely aligned with the Federal Government, demonstrate that the Supreme Court has drawn away from the concept of absolute tax immunity based solely upon federal instrumentality status.

PCA correctly points out that the language with respect to federal instrumentalities quoted from ***United States v. New Mexico*** is dicta, since it is undisputed that the entities taxed in

that case were federal contractors, and not federal instrumentalities. While the trend in twentieth century federal jurisprudence with respect to intergovernmental tax immunity has clearly been to narrow the breadth of the tax immunity of entities associated with the Federal Government, and while courts often use dicta to foreshadow trends in jurisprudence, the fact remains that there are no reported decisions which have restricted the immunity of federal instrumentalities based upon an insufficient congruency in the activities and powers of the instrumentality and the Federal Government itself. The State of Arkansas raised the identical argument in its dispute with the Arkansas Production Credit Associations and the argument was rejected by both the Eighth Circuit Court of Appeals and the Chancery Court of Pulaski County, Arkansas. In the absence of any authority which distinguishes the tax immunity of federal instrumentalities based upon how closely their activities are connected to those of the Federal Government, the Department's argument must be rejected.

This leaves us with the primary issue presented by this case. PCA argues that federal instrumentality status is talismanic with respect to immunity from state taxes in the absence of congressional authorization to tax. PCA maintains that because the the 1985 amendments to the Farm Credit Act removed the congressional authorization, the imposition of state income tax is clearly prohibited by a line of federal jurisprudence unbroken since ***McCulloch v. Maryland, supra***. The Department argues that it would ignore congressional intent to apply immunity from state income taxes to production credit associations given the legislative history of the federal statutes addressing the tax immunity of those entities.

Were we to engage in an effort to discern congressional intent behind the 1985 amendments to Section 2077, I have no doubt that Congress did not intend to confer state income tax immunity upon production credit associations by the amendments. Since at least 1968, there

have been no production credit associations immune from state income taxes under the language omitted by the 1985 amendments because there were no longer any production credit associations whose stock was wholly or partially owned by the Federal Government. The House Report on the amendments makes no reference to the removal of the language addressing exemption from tax, referring to the amendments as merely "technical" and "conforming" amendments consistent with the purpose of the 1985 amendments to restructure the Farm Credit Administration. Thus, the reference to the "Governor of the Farm Credit Administration" in the last sentence of Section 2077, which limited the exemption from tax to production credit associations whose stock was held by the Governor of the Farm Credit Administration was no longer needed because the amendments restructured the Farm Credit Administration and did away with the Governor's position.

Not only were there no production credit associations that qualified for the waiver of tax immunity contained in Section 2077 when the language conferring it was removed in 1985, but that waiver of immunity had been part of the federal statutes since production credit associations were created by the Farm Credit Act of 1933. In fact, the federal scheme with respect to taxation of production credit associations had never relied upon the implied tax immunity conferred upon federal instrumentalities to confer such tax immunity. Since their creation, Congress provided an express statutory exemption from tax for production credit associations and limited the exemption to those production credit associations which were either partially or wholly owned by the Federal Government. It would defy all logic to conclude that somehow, by removing an exemption from tax and a limitation on that exemption that had been part of the federal scheme for production credit associations for more than fifty years, but was no longer applicable, that Congress intended to create an implied common law tax immunity which had never been part of

the federal scheme from the outset. To further conclude that Congress did this without a single mention or acknowledgement of this result anywhere in the legislative history pushes legal reasoning beyond reason and into the realm of absurd and unintended results.

We are thus left to choose between two legal doctrines, both of which are so well established and founded upon sound legal reasoning as to be beyond challenge as to their propriety, but which lead to diametrically opposing results. PCA argues that ***McCulloch v. Maryland*** and 179 years of unwavering federal jurisprudence under the Supremacy Clause dictates that the imposition of New Mexico's tax be barred. The Department argues that this result in contrary to the intent of Congress behind the 1985 amendments to the Farm Credit Act and that in construing the effect of amendments to statutes, the legislative intent must govern our determination. While both sides have done an excellent job in arguing the merits of their respective positions, neither have presented a conceptual basis which can reconcile the two conflicting legal doctrines and provide a persuasive basis as to which approach should govern this determination. For that matter, the parties in the parallel litigation in the federal courts and now the courts of Arkansas have similarly failed to come up with an approach which provides a rationale to harmonize the conflicting approaches to the resolution of this issue.

To resolve this quandry, we must examine the conceptual underpinnings of the federal instrumentality tax immunity doctrine and examine the appropriateness of applying the doctrine to the facts of this case. We must bear in mind that from the outset, the doctrine of immunity for federal instrumentalities has been a doctrine of *implied* immunity. As noted by Professor Tribe in his discussion of the development of the intergovernmental immunity doctrine:

> ***McCulloch*** thus announced the prophylactic per se rule that has been followed ever since. If Congress does not authorize state taxation or regulation of Federal instrumentalities, *the possibility of*

> *interference with substantive federal policy is sufficient to raise a presumption of immunity.*

Laurence H. Tribe, ***Intergovernmental Immunities in Litigation, Taxation and Regulation: Separation of Powers Issues in Controversies About Federalism***, 89 Harv. L.R. 682, 701 (1976)(emphasis added). Thus, immunity is implied because of a presumption of interference in the absence of a congressional expression which addresses the state-federal balance.

One is led to inquire, then, on what conceptual basis can we apply a doctrine of intergovernmental tax immunity whose underpinnings rest upon an implied immunity based on congressional silence to federal instrumentalities whose tax immunity was *never* dependent upon such implied immunity? As noted earlier herein at pp. 10-13, since their creation, the tax immunity of production credit associations was expressly stated and expressly limited by explicit congressional enactments. Even to this day, the exemption from taxation for the notes, debentures, bonds and other obligations of production credit associations remains express, rather than implicit. 12 U.S.C. § 2077. Congress has not been silent with respect to the taxability of production credit associations. Under these circumstances, it makes no sense to blindly apply a doctrine of implied immunity developed and intended to apply when Congress has been silent, to create an immunity from state income taxes which the legislative history of the applicable federal statutes clearly demonstrates was never intended to apply to privately owned production credit associations. Rather, we should look to the congressional intent behind the 1985 amendments to determine whether Congress intended to confer an immunity from state income taxes upon privately owned production credit associations. If we do so, it is clear that no such intent to confer immunity existed.

Although it is noted that this approach to the tax immunity of production credit associations relies upon distinguishing the treatment of these federal instrumentalities from those where there has not been an express congressional waiver of immunity and a subsequent amendment to that waiver, this approach to the issue of intergovernmental immunity does no violence to the underlying concept of implied immunity. Since ***McCulloch v. Maryland,*** the Court has noted that Congress is best situated to determine the circumstances under which a state tax interferes with the execution of federal policy, ***Id.,*** 17 U.S. at 431, and in the absence of such a determination, immunity would be implied. In this case, where Congress stated that there would be no state income tax immunity for privately owned production credit associations, it does no violence to the balance of power between the States and the Federal Government to look to the intent of Congress when it enacted the 1985 amendments to the Farm Credit Act to determine whether Congress intended to confer a level of state tax immunity which had not heretofore existed for privately owned production credit associations.

CONCLUSIONS OF LAW

1. PCA filed timely protests to the Department's denials of its claims for refund of corporate income tax for the 1992-1996 tax years and jurisdiction lies over both the parties and the subject matter of this protest.

2. PCA is a federal instrumentality.

3. Since the creation of production credit associations by the Farm Credit Act of 1933, Congress expressly waived the immunity of privately owned production credit associations from the imposition of state income taxes upon their income.

4. Congress did not intend, by the enactment of the Farm Credit Amendments Act of 1985, to confer an implied immunity from state income taxes for privately owned production credit associations.

5. PCA is not immune from the imposition of New Mexico Corporation Income Tax under the Supremacy Clause of the United States Constitution.

For the foregoing reasons, the protest of PCA IS HEREBY DENIED.

DONE, this 21st day of December, 1998.