

BEFORE THE STATE BOARD OF EQUALIZATION

FOR THE STATE OF WYOMING

IN THE MATTER OF THE APPEAL OF)
PATRIOT ENERGY RESOURCES LLC)
FROM A DECISION BY THE DEPARTMENT) Docket No. 2012-24
OF REVENUE (Production Audit 2007-2009))

DECISION AND ORDER

APPEARANCES

Walter F. Eggers, III, P.C., and Lawrence J. Wolfe, P.C., Holland & Hart LLP, appeared on behalf of Petitioner, Patriot Energy Resources LLC (Patriot).¹

Karl Anderson, Senior Assistant Attorney General, and John G. Knepper,² Senior Assistant Attorney General, Wyoming Attorney General's Office, appeared on behalf of the Wyoming Department of Revenue (Department).

STATEMENT OF THE CASE

The Department determined that natural gas producer Patriot had undervalued its production and subsequent sale of natural gas to United Energy Trading (UET) from July 1, 2008, through June 30, 2009. The Department based this decision on an audit conducted by the Department of Audit (DOA) showing Patriot received additional income from UET. Accordingly, the Department assessed Patriot \$229,896.60 in additional severance tax and \$79,824.00 in related interest calculated through February 11, 2012.

Patriot appealed the additional assessment and interest contending that it properly

¹ On March 27, 2015, Mr. Eggers and Holland & Hart, LLP, filed a Motion for Leave to Withdraw as Counsel, alleging in part, that "Patriot and its parent company no longer exist." (Mot. for Leave to Withdraw as Counsel, ¶ 3). Counsel also alleged a conflict of interest from a case unrelated to the appeal. *Id.* at ¶ 4. The State Board granted the Motion on April 16, 2015. As of the date of this Order, neither a successor in interest nor substitute counsel have entered an appearance of record.

² Mr. Knepper filed a Notice of Withdrawal of Co-Counsel on February 6, 2013.

paid taxes for its Campbell County mineral production based on average Gas Daily prices, pursuant to a written contract between Patriot and UET. Patriot contended that the additional income it received from UET was pursuant to a separate financial agreement, which UET and Patriot referred to as a “hedge agreement” (Hedge or Hedge Agreement). Patriot claimed that the Hedge did not involve the purchase, sale or physical delivery of gas, and consequently, it argued it did not owe severance tax or interest on the income from the Hedge. (Pet’r’s Updated Summ. of Contentions 2; Wyo. Dep’t of Revenue’s Updated Summ. of Contentions 2-3).

The Department responded that the Hedge Agreement and the Gas Purchase Agreement were integrated transactions for the purchase of Patriot’s gas. The Department argued the valuation statutes required it to consider all transactions between the parties, including the Hedge, to capture the full fair market value that Patriot received from UET for its production. (Wyo. Dep’t of Revenue’s Updated Summ. of Contentions 2).

The Wyoming State Board of Equalization (State Board) held a hearing on February 12-13, 2013. The State Board,³ comprised of Chairman E. Jayne Mockler, Vice Chairman Martin L. Hardsocg, and Board Member Robin Sessions Cooley, considered the record of the proceedings including the transcript, exhibits, and various pleadings. Upon this consideration, the State Board affirms the Department’s January 12, 2012, Final Determination.

JURISDICTION

The State Board shall review final decisions of the Department on the application of any interested person adversely affected. Wyo. Stat. Ann. §§ 39-11-102.1(c) (2011); Wyo. Stat. Ann. § 39-14-309(b)(iv) (2011). Taxpayers are specifically authorized to appeal final decisions of the Department, but the appeal must be filed with the State Board within thirty days of the Department’s final decision. Wyo. Stat. Ann. § 39-14-309(b) (2011); Rules, Wyo. State Bd. of Equalization, ch. 2 § 5(a) (2006). Patriot filed its Notice of Appeal February 10, 2012, within thirty days of the Department’s January 12, 2012, Final Determination. Accordingly, the State Board has jurisdiction to hear and decide this matter.

³ Paul Thomas Glause and Steven D. Olmstead were members of the State Board when Patriot initially filed the appeal. Mr. Glause resigned from the State Board, effective January 2, 2015. Mr. Olmstead’s term on the State Board expired on March 1, 2015. Governor Matthew H. Mead appointed Robin Sessions Cooley and Martin L. Hardsocg to the State Board effective March 16, 2015.

FINDINGS OF FACT

Patriot's Evidence

A. Introduction – Patriot/Luca

1. Patriot is a wholly owned subsidiary of Luca Technologies, Inc. (Luca). Patriot holds all of Luca's oil and gas producing assets. (Tr. vol. I, 35, 46-49; Ex. 101).
2. Luca's Chief Operating and Financial Officer, Brian Cree, testified on behalf of Patriot. Mr. Cree testified to his knowledge of Luca and Patriot, including their acquisition of the gas wells involved in this case. Mr. Cree testified to Patriot's payment of severance and ad valorem taxes and to all transactions related to UET at issue in this appeal. (Tr. vol. I, 32-214).
3. Tom Williams, President and partial owner of UET, also testified on behalf of Patriot. Mr. Williams testified to the gas sale/purchase contracts, and to the transportation, marketing, and hedge transactions between Patriot and UET. (Tr. vols. I-II, 215-80).

B. Production Process

4. Patriot is or was at the time of hearing, an oil and gas production company attempting to use biotechnology to create and produce natural gas from previously producing wells through the bio-conversion of organic substrates, such as coal, into natural gas. (Tr. vol. I, 38-40).
5. Patriot intended to inject extracted well water back into well bores, where the organisms in the water would then regenerate natural gas production. Patriot proposed to feed these organisms with certain nutrients, accelerating and stimulating the organisms to more effectively produce gas and increase production in wells near the end of their useful lives. This process would allow the wells to continue producing for 50 or more additional years. In Patriot's words, it sought to create "natural gas farms" to "grow[] gas for a long time." (Tr. vol. I, 39-44).

C. Patriot Acquisitions from 2007 – 2008 and the Base Contract

6. In three separate transactions, Patriot acquired 1,350 gas wells in Campbell County, Wyoming. Only two of these acquisitions occurred during the relevant audit time period. (Tr. vol. I, 48-49; Ex. 101).
7. On November 29, 2007, in the first of those two acquisitions, Patriot acquired the assets of Patriot Production, LLC (Patriot Production), including 100 gas wells in the

“Terra” and “Pronghorn” fields. That acquisition included an existing gas purchase agreement with UET dated June 27, 2006. The parties referred to this gas purchase agreement as the Base Contract; it established the initial foundation for Patriot’s gas sales to UET. The Base Contract set a “spot price standard” for the gas sale. (Tr. vol. I, 48, 66-67; Exs. 507, 705). Mr. Cree defined “spot price” as market value on a given day. *Id.* The Base Contract defined “Spot Price” as “the price listed in the publication indicated on the Base Contract, under the listing applicable to the geographic location closest in proximity to the Delivery Point(s) for the relevant Day[.]” (Ex. 507 at 152).

8. In this same transaction, Patriot also acquired a transportation agreement between Patriot Production and UET, dated August 17, 2007, which provided Patriot Production transportation rights using UET’s pipeline capacity, to transport 400 MMBtu⁴ per day of Patriot Production’s gas. This transportation agreement ran from October 1, 2007, through May 31, 2009. In sum, when Patriot acquired Patriot Production’s wells, it also assumed a gas purchase agreement (Base Contract) and a transportation agreement with UET relating to these 100 gas wells. (Tr. vol. I, 46-68, 219; Exs. 101-102, 507).

9. The Base Contract provided the standard terms between Patriot and UET, but the parties orally agreed upon gas volumes, sales durations, and the spot daily pricing, followed by written transaction confirmations to confirm the oral agreements. The testimony indicated that these types of oral agreements, followed by written confirmations, are not unusual in the oil and gas industry. (Tr. vol. I, 64-66; Exs. 507 at 151, 707 at 48, 714 at 112).

10. Patriot next acquired 525 gas wells from Kennedy Oil Corporation (Kennedy Oil) on June 2, 2008. The parties referred to these wells, also located in Campbell County, Wyoming, as the “North Kitty,” “Central Kitty,” “West Kitty,” “South Kitty,” and “Recluse” fields. The Kennedy Oil acquisition included a transportation contract with yet another company. (Tr. vol. I, 54; Exs. 101-102).

D. Financial Hedge Agreement dated June 25, 2008

11. The Kennedy Oil acquisition cost Patriot approximately ten million dollars. Mr. Cree testified that this significant expenditure caused Patriot to begin looking for additional ways to generate revenue. (Tr. vol. I, 54-56, 82-83).

⁴ “MMBTU” is defined in the Base Contract as “one million British thermal units, which is equivalent to one dekatherm.” (Ex. 507 at 152).

12. To generate additional revenue, Patriot approached various entities seeking what it referred to as a Hedge Agreement. Patriot believed this type of agreement would guarantee a more predictable revenue stream to protect against price fluctuations in the natural gas market. (Tr. vol. I, 55-56, 82-84). Mr. Cree testified that “during the month of June we looked at different ways to put in place a financial transaction at a corporate level that would guaranty cash back to help pay for [the Kennedy Oil purchase]. And so during the course of June we went out and spoke to many different entities about the possibility of putting in place a financial transaction that would allow us to get a return on our investment, or protect our investment in those assets.” (Tr. vol. I, 56).

13. Mr. Cree and Mr. Williams both explained their understandings of hedge agreements, testifying that the purpose of such an agreement is to reduce the risk of adverse price movements in an asset, in this case, natural gas. They explained that a hedge typically consists of a party taking an offsetting position in a related security, such as a futures contract. They both recognized that these agreements are usually with banks and are not generally tied to the physical production and extraction of natural gas. (Tr. vol. I, 84-85, 251-52).

14. Mr. Cree did not believe Patriot had sufficient collateral, due to its recent gas well purchases, to support this type of hedge agreement with a bank, so he sought such an agreement with two other gas trading companies. Both of these companies declined Patriot’s hedge proposal. (Tr. vol. I, 84–90; Exs. 718, 724).

15. Because of its existing relationship with UET under the Base Contract and the transportation agreement, Patriot next approached UET about the possibility of entering into a hedge agreement. *Supra* ¶¶ 7-9. UET agreed and in June 2008, the parties entered into what they referred to as a Hedge Agreement. At that time, Patriot was still selling and transporting a portion of its Patriot Production gas through UET under the Base Contract Patriot assumed upon its purchase of the Patriot Production wells. (Tr. vol. I, 56-57, 62, 90-92, 221-23; Ex. 507).

16. On June 25, 2008, Patriot and UET confirmed the Hedge Agreement in a standard gas sale/purchase transaction confirmation form (Hedge Confirmation) the parties generally used to document a gas sale/purchase transaction confirmation. Because Patriot and UET documented the Hedge on a gas sale/purchase transaction confirmation form, it looked like a gas sale/purchase transaction. That confirmation identified the following: the length of the agreement from July 1, 2008, to June 30, 2009; the firm fixed price of \$9.38; the UOM or unit of measurement of 2,000 MMBtu per day; and it identified the meter location as the WIC⁵ Medicine Bow. It further stated that the “[p]rice will be

⁵ WIC refers to the Wyoming Interstate Gas Company. The WIC Medicine Bow refers to the pipeline going through Medicine Bow. (Tr. vol. I, 228-29).

adjusted to Cheyenne Hub premium less transportation costs and a negotiated marketing fee[]” and that “[t]his Transaction Confirmation is subject to the terms and conditions of the Base Contract between Seller and Buyer dated October 24, 2007.” (Ex. 706).

17. Mr. Cree and Mr. Williams explained that the Hedge Confirmation looked like a gas sale/purchase because UET’s computer system did not include terms generally associated with financial agreements. In fact, Mr. Cree agreed that numerous terms in the document were not correct, or he did not know what they were because the document originated with UET. However, Mr. Cree never filed a written dispute with UET over these terms, stating he had no reason to because he did not get this document until four months after the parties entered into the financial agreement and he had already received four months of payments under the agreement. (Tr. vol. I, 90-103, 154-63, 224-30; Exs. 506-507, 705 at 26, 706, 715, 723).

18. Attempting to explain why the Hedge Confirmation contained gas sale/purchase terms, Mr. Williams stated the WIC Medicine Bow meter location either identified a physical location or provided a price basis in that area, but he never indicated which applied to the Hedge Confirmation. Neither was there sufficient explanation of why the Hedge Confirmation indicated that the “[p]rice will be adjusted to Cheyenne Hub premium less transportation costs and a negotiated marketing fee[]” or that the Hedge Confirmation was subject to the Base Contract. (Tr. vol. I, 228-29; vol. II, 249-50; Ex. 706).

19. Mr. Cree testified the parties orally agreed to compare the \$9.38 firm fixed price against an IFERC price to determine the hedge outcomes, but there is nothing in writing to confirm the IFERC as the “settlement” price. (Tr. vol. I, 169-70; vol. II, 248-50). Mr. Cree identified the IFERC as “an industry price that is set and used for these type of transactions.” (Tr. vol. I, 93). The only document that references the IFERC is an internal spreadsheet drafted by Patriot to help document the various exchanges. (Ex. 506).

20. Mr. Cree explained that the Hedge Agreement required that if the IFERC first of month published price moved above \$9.38, Patriot would pay UET and, conversely, if the IFERC price moved below \$9.38, Patriot would receive the difference in payment from UET. (Tr. vol. I, 93-95). Providing an example of how the Hedge Agreement was calculated, Mr. Cree explained that using the month of September, which is a 30 day month, 2,000 MMBtu per day would be equivalent to 60,000 MMBtu per month. Patriot would compare the \$9.38 hedge price to the IFERC industry price on the first day of the month. If the IFERC price was lower than \$9.38, UET would pay Patriot the difference. If the IFERC price was higher than \$9.38, Patriot would owe UET the difference. (Tr. vol. I, 93). Mr. Williams testified that after entering into this Hedge Agreement with Patriot, UET entered into a subsequent similar transaction of its own with another entity. (Tr. vol. I, 230-32; Ex. 100).

21. Patriot conceded, and UET confirmed, that even though these two companies had a contract for the sale/purchase of gas, and for the transportation and marketing of gas, they did not have a written contract outlining the terms of the Hedge Agreement. (Tr. vol. I, 95-96, 169-73, vol. II 248-49, 277). Mr. Cree simply stated “It’s part of the relationship that we have with - - with UET.” (Tr. vol. I, 169). He continued to reiterate that it was simply “the understanding that [the parties] have[.]” (Tr. vol. I, 170).

22. Mr. Cree and Mr. Williams both testified the Hedge Agreement had nothing to do with the purchase, sale or physical delivery of gas between these parties from July 1, 2008, through June 30, 2009. If Patriot produced no gas in a given month, the parties would still make the hedge calculation to determine whether Patriot owed UET or vice versa. Patriot and UET would apply the difference between the \$9.38 and the IFERC first of month price to the financial volume of 2,000 MMBtu, multiplied by the number of days in the month, to make this calculation and to determine which party owed the other. Both Patriot and UET claimed the Hedge Agreement was a financial agreement based on gas price movements, and that it did not rely on the actual production and sale of gas. They further explained that gas terms are used in the Hedge simply as mechanisms to determine amounts owed and under what circumstances. (Tr. vol. I, 93-97, 225, 233-36).

23. Mr. Williams unequivocally testified, however, that it was his confidence in Patriot’s ability to physically produce more than 2,000 MMBtu of gas per day to cover any of Patriot’s Hedge losses that allowed him to agree to the Hedge. Mr. Williams conceded, in fact, that the gas purchase agreement, discussed below, wherein Patriot agreed to sell all of its gas production to UET, and the financial agreement were integrated transactions – one would not happen without the other. (Tr. vol. I, 222-25, 233-34; vol. II, 242-47, 256, 270-71).

E. Gas Sale/Purchase, Transportation and Marketing Letter Agreement dated July 1, 2008

24. The parties also renegotiated the Base Contract while negotiating the Hedge Agreement. Patriot and UET replaced the Base Contract with a Gas Purchase and Transportation Letter Agreement (Gas Purchase Agreement) on July 1, 2008, just shortly after confirming the Hedge Agreement terms on June 25, 2008. Mr. Williams testified that in exchange for agreeing to the Hedge, Patriot and UET entered into a Gas Purchase Agreement which required Patriot to sell UET all of the gas it produced at a fixed price, for a fixed term. (Tr. vol. I, 68, 71-74, 175, 222-23; vol. II, 242-47, 258-60; Exs. 102, 507, 720). Patriot and UET recognized that UET would not have entered into the Hedge Agreement in June 2008, without also securing physical delivery of all of Patriot’s gas production under the Gas Purchase Agreement. *Id.* Mr. Williams testified that he agreed to the Hedge because of, or in exchange for, the ability to “manage” all of Patriot’s gas volumes as collateral; one was consideration for the other. (Tr. vol. II, 242). He was

confident Patriot would produce three to four times the required volumes of gas for a cash offset if needed. (Tr. vol. II, 242-50, 256-58; Exs. 102, 706, 720).

25. Mr. Cree and Mr. Williams also testified to the parties' record keeping of these various agreements and the overall transactions. The records documenting the Gas Purchase Agreement exchanges and the Hedge Agreement terms and exchanges were identical because UET's computer system was not set up to recognize a distinction between these two types of transactions. In addition, UET invoiced and paid amounts owed for the physical sale of gas and under the financial agreement in combined invoices, confusing the accounting further. Without the additional testimony from Mr. Cree to explain the documentation and the terms, the hedge exchanges looked identical to the gas sales and purchases. (Tr. vol. I, 107-17, 227; vol. II, 245-50).

26. The only apparent tracking of the amounts owed under the Hedge Agreement was on an internal spreadsheet, drafted by Patriot, and reviewed for accuracy by UET. The spreadsheet shows the agreed upon volume per day of 2,000 MMBtu, the days in the month, the IFERC first of month price, the hedge price, the price difference and the amount due by whichever party owed the other for that month. There is also a price breakdown by day of the month. There is no date identifying when Patriot created the spreadsheet, nor do the documents reveal that the parties agreed upon these amounts. (Ex. 506). Exhibit 506 is the Hedge accounting spreadsheet for the months of July 2008, through June 2009. Mr. Cree testified that Patriot only implemented this method when it questioned the amount received from UET under the Hedge terms. (Tr. vol. I, 118-20, 210; Ex. 506).

27. Adding to the confusion caused by its record keeping, Patriot treated the Hedge Agreement as a physical sale of gas in its consolidated financial statement. The financial statement provided:

Commodity Contracts.

The Company periodically uses derivative financial instruments to achieve a more predictable cash flow from its gas production by reducing its exposure to natural gas price fluctuations. **In 2008, the Company entered into physical commodity contracts with its gas purchaser for the sale of 2,000 MMBtu per day of natural gas from July 2008 through June 2009 at a price of \$9.38 per MMBtu.** The Company's natural gas derivative financial instruments are accounted for in accordance with ASC 815, *Derivatives and Hedging*. The Company has elected the normal purchase and sale exception permitted under ASC 815 and accordingly was not required to apply its provisions to the fixed-price gas contracts. As a result, no asset or liability has been recorded for the fair value of these contracts in

the accompanying consolidated balance sheets of the Company. As of December 31, 2010 and 2009, no derivative contracts were in place.

(Ex. 712 at 95-96) (emphasis added).

28. The financial statement refers to a “commodity contract[.]” for the “sale” of gas from July 2008 through June 2009, at \$9.38 per MMBtu. *Id.* Mr. Cree recognized that Patriot’s argument that the Hedge was strictly a financial transaction was not “absolutely consistent” with the language in the financial statement. (Tr. vol. I, 197). He testified, however, that Patriot identified the Hedge Agreement as a physical sale in its financial statements believing that this identification would be easier for its investors to understand. Patriot identified the contract to investors as a gas sale even though its internal auditors initially advised it to identify the Hedge as a financial hedging transaction. (Tr. vol. I, 187-98; Ex. 712 at 95-96).

29. Mr. Cree testified that during the audit time period, Patriot reported ad valorem and severance taxes on the market value of the gas that it physically delivered and sold to UET. (Tr. vol. I, 81).

Department of Revenue’s Evidence

A. DOA Findings

30. The DOA engaged Patriot in an audit covering production years 2007 through 2009. Derek Weekly, the Audit Manager with the DOA, supervised the staff conducting the audit. (Tr. vol. II, 281-408).

31. The DOA conducted the audit using the netback formula found in Wyoming Statutes section 39-14-203(b)(vi)(C) (2009). This statute requires the DOA to determine the fair market value of the gas by looking at the sales price minus certain expenses. (Tr. vol. II, 285-87, 411-15).

32. The DOA examined Patriot’s records to determine whether Patriot accurately reported and paid severance taxes to the State of Wyoming. Mr. Weekly testified that, for the DOA to accurately determine sales price, it must consider all relevant and available contracts, confirmation transactions, invoices, remittances and wire transfers or checks received. (Tr. vol. II, 287-92, 328-34, 412-15). These documents allow the DOA to “complete the circle” to confirm their findings regarding all relevant transactions. (Tr. vol. II, 290).

33. Mr. Weekly testified that, during an audit, auditors generally see multiple purchasers buying gas from a single producer. Because of the various entities involved,

auditors are usually required to review and audit multiple agreements and contracts. The DOA found the Patriot audit uncommon because the auditors only reviewed documents between Patriot and UET. The auditors did not find documentation involving multiple entities because the Gas Purchase Agreement required Patriot to sell all of its gas to UET. (Tr. vol. II, 287-88, 354).

34. According to Mr. Weekly, it is also very common in an audit to see multiple components of a sales price and to find consideration for the sale that goes beyond what is found in the contract. (Tr. vol. II, 287-90). He testified that Wyoming Statutes defining “sales price” require auditors to “look at all transactions of cash and equivalence to cash in order to come up with a market value.” (Tr. vol. II, 289). “[T]here are times that you have to look further than just one piece of the transaction.” *Id.*

35. After considering the documents Patriot provided, the DOA issued a Preliminary Issue letter finding that Patriot had undervalued its reported pricing from July 1, 2008, through June 30, 2009. The DOA found that Patriot calculated and reported the difference between the total money received and an average Gas Daily price. Patriot responded that the compensation exceeding the Gas Daily price resulted from the Hedge Agreement. Patriot argued that because the Hedge income had nothing to do with the gas sale/purchase, it was not subject to taxation. (Tr. vol. II, 293-301; Exs. 501, 506, 702-703).

36. In response to Patriot’s claim, the DOA requested that Patriot provide it with the Hedge Agreement to support its position. Patriot could not produce a written contract, providing only a sales confirmation document and an internal spreadsheet. (Exs. 706, 506). Patriot offered no explanation of the spreadsheet during the audit, other than to say it provided the “weighted-average price” or the “hedge profit.” (Tr. vol. II, 298). For this reason, and because they did not believe it was necessary, the auditors did not give much consideration to the spreadsheet. (Tr. vol. II, 366-67; Ex. 506). The auditors instead focused on the Hedge Confirmation, tying it to invoices and payments through the transaction identification numbers on the documents. (Tr. vol. II, 366-400; Ex. 706).

37. On several occasions, the DOA requested additional information from Patriot in response to its claim the additional income resulted from a separate financial agreement, but received minimal documentation from Patriot that was relevant to the request. (Tr. vol. II, 298-305, 350, 366; Exs. 507, 705).

38. For instance, the DOA did not receive the entire Base Contract or the Gas Purchase Agreement that superseded it until Patriot exchanged its proposed exhibits with the Department in preparation for the hearing, despite several earlier requests for the documentation. (Tr. vol. II, 293-318; Exs. 506, 720).

39. Further, the DOA learned specifics about how Patriot identified and treated the Hedge income and how it handled the record keeping for the first time at the hearing. (Tr. vol. II, 299).

40. Ultimately, the DOA found that Patriot's documentation revealed a fixed price contract. The DOA confirmed its preliminary conclusions, finding that Patriot had undervalued its reported pricing from July 1, 2008, through June 30, 2009. (Tr. vol. II, 311-18, 323; Exs. 501, 505, 706).

B. Department of Revenue Findings

41. Craig Grenvik, Mineral Tax Division Administrator with the Department of Revenue (Department) and a former auditor with the DOA, testified to the Department's review of the DOA's audit findings, and to the reasons for its decision to assess additional severance tax and interest. He explained that the Department assessed taxes on Patriot's gas production using the "netback" valuation method. (Tr. vol. II, 411). The Department interprets the term "sales price" used in the netback statutes to mean the "transaction price" which is the price applied to the volumes considering all the transactions involved with the sale. (Tr. vol. II, 412) (Tr. vol. II, 408-41).

42. Mr. Grenvik testified that he had seen various hedge agreements, but the Department was not generally concerned with them because they were with banks and were not between the producer and the seller, nor were they tied to production. (Tr. vol. II, 416-21).

43. Mr. Grenvik testified that this transaction was different for a number of reasons. First, the agreement was not with a bank, it was with a purchaser who was actually buying, marketing and transporting the producer's gas. Second, the Hedge Agreement is shown on invoicing documents that are generally applicable to gas volumes actually produced. (Tr. vol. II 418-19). Finally, Mr. Grenvik testified the Hedge is "tied to volumes in question here because depending upon the level of . . . nondelivery, that impacts the price that's actually -- the value that's actually being realized by Patriot here." (Tr. vol. II, 419). He believed the Hedge Agreement between Patriot and UET was tied to gas production because that production would ultimately impact the price or the value realized by Patriot. (Tr. vol. II, 417-20).

44. Mr. Grenvik further testified that it is "virtually unheard of not to have complete documentation . . . in a contractual format for your pricing mechanisms, your processing arrangements, your transportation arrangements." (Tr. vol. II, 421). He testified that the Department is concerned that oral contracts like these allow parties to agree on pricing structures that could never be tied back to the company or to its production. (Tr. vol. II, 421-22, 435-37).

45. The Department reviewed and adopted the DOA's findings on January 12, 2012, the same date the DOA issued its final determination letter. (Tr. vol. II, 411; Exs. 700-703). In its assessment, the Department treated Patriot's alleged hedge income as a physical sale of gas because it had no way to determine otherwise from the documentation or information provided by Patriot. (Tr. vol. II 411-21; Exs. 700-701). That is, the Hedge Agreement records were identical to the records tracking physical sales of gas between Patriot and UET, and no Hedge Agreement contract existed between the parties. (Tr. vol. II, 299, 316-18, 346, 366-68; Exs. 501 at 51, 506).

46. Any portion of the Conclusions of Law – Principles of Law, or the Conclusions of Law – Application of Principles of Law, set forth below that include a finding of fact not included above may also be considered a State Board Finding of Fact and, therefore, is incorporated herein by this reference.

CONCLUSIONS OF LAW – PRINCIPLES OF LAW:

A. Burden of proof:

47. “Any person aggrieved by any final administrative decision of the department may appeal to the state board of equalization.” Wyo. Stat. Ann. § 39-14-209(b)(i) (2009).

48. The role of the State Board in this matter is to adjudicate the dispute between the parties.

It is only by either approving the determination of the Department, or by disapproving the determination and remanding the matter to the Department, that the issues brought before the Board for review can be resolved successfully without invading the statutory prerogatives of the Department. The statutory mandate to the Board is not to maximize revenue or to punish nettlesome taxpayers, but to assure the equality of taxation and fairly adjudicate disputes brought before it.

Amoco Prod. Co. v. Wyo. State Bd. of Equalization, 12 P.3d 668, 674 (Wyo. 2000).

49. “[T]he burden of proof with respect to tax valuation is on the party asserting an improper valuation.” *Williams Prod. Co. v. State Dep’t of Revenue*, 2005 WY 28, ¶ 7, 107 P.3d 179, 183 (Wyo. 2005) (citations omitted). More specifically, the State Board Rules provide:

Except as specifically provided by law or in this section, the Petitioner shall have the burden of going forward and the ultimate burden of persuasion, which burden shall be met by a preponderance of the evidence. If Petitioner provides sufficient evidence to suggest the Department determination is incorrect, the burden shifts to the Department to defend its action.

Rules, Wyo. State Bd. of Equalization, ch. 2 § 20 (2006).

50. A preponderance of the evidence is “ ‘proof which leads the trier of fact to find that the existence of the contested fact is more probable than its non-existence.’ ” *Kenyon v. State, ex rel., Wyo. Workers’ Safety & Comp. Div.*, 2011 WY 14, ¶ 22, 247 P.3d 845, 851 (Wyo. 2011) (citations omitted).

B. Legal review principles:

51. The State Board is required to “[d]ecide all questions that may arise with reference to the construction of any statute affecting the assessment, levy and collection of taxes, in accordance with the rules, regulations, orders and instructions prescribed by the department...[u]pon application of any person adversely affected[.]” Wyo. Stat. Ann. § 39-11-102.1(c)(iv)(A) (2009).

52. The State Board’s main task in this matter is to interpret various statutory provisions and to determine if the Department correctly applied those provisions to the facts. Statutory interpretation is a question of law that is reviewed de novo. *Powder River Coal Co. v. Wyo. State Bd. of Equalization*, 2002 WY 5, ¶ 6, 38 P.3d 423, 426 (Wyo. 2002) (citation omitted).

53. The principles of statutory interpretation are well-defined:

When interpreting statutes, we follow an established set of guidelines. First, we determine if the statute is ambiguous or unambiguous. A statute is unambiguous if its wording is such that reasonable persons are able to agree as to its meaning with consistency and predictability. Unless another meaning is clearly intended, words and phrases shall be taken in their ordinary and usual sense. Conversely, a statute is ambiguous only if it is found to be vague or uncertain and subject to varying interpretations.

If a statute is clear and unambiguous, we give effect to the plain language of the statute. To determine whether a statute is ambiguous, we are not limited to the words found in that single statutory provision, but may consider all

parts of the statutes on the same subject. If a statute is ambiguous, we may resort to principles of statutory construction to determine the intent of the legislature.

Exxon Mobil Corp. v. Dep't of Revenue, 2009 WY 139, ¶ 11, 219 P.3d 128, 134 (Wyo. 2009) (citations omitted).

54. In interpreting statutes, the State Board will give deference to the statutory interpretation of an agency charged with the administration of those statutes unless that interpretation is clearly erroneous. *Parker Land and Cattle Co. v. Wyo. Game and Fish Comm'n*, 845 P.2d 1040, 1045 (Wyo. 1993).

C. Application of law to the facts:

55. The primary question the State Board must answer is whether Patriot presented sufficient credible evidence to prove by a preponderance of the evidence that the Department erred in assessing additional severance taxes and interest against Patriot for production years 2007 through 2009. In answering this question, the State Board must first decide whether Patriot established that it is more likely than not that Patriot entered into a Hedge Agreement with UET. If the State Board finds that Patriot established such a Hedge Agreement with UET, the State Board must then decide whether the mineral valuation statutes authorized the Department to include the income Patriot realized from the Hedge Agreement into the “sales price” of its gas production for severance tax purposes.

1. Did Patriot establish it had entered into a Hedge Agreement with UET?

56. The severance taxation of mine products in Wyoming is self-reported. Wyo. Stat. Ann. § 39-14-207 (2011); *Moncrief v. Wyo. State Bd. of Equalization*, 856 P.2d 440, 445 (Wyo. 1993) (“Since the severance tax was enacted in 1969, it has been a self-assessment system.”).

57. The DOA is authorized to conduct audits of taxpayer-reported values “for the collection of federal and state mineral royalties and for collection of taxes imposed under Title 39, Wyoming Statutes[.]” Wyo. Stat. Ann. § 9-2-2003(e) (2009). The purpose of an audit is to ensure severance tax is properly reported and paid. Wyo. Stat. Ann. § 39-14-208(b)(ix) (2009).

58. The Department may request that the DOA conduct an audit, involving the examination of “the books and records of any person paying ad valorem taxes,” to verify a taxpayer's reported values. Wyo. Stat. Ann. § 39-14-208(b)(i) (2009). The Department is

entitled to rely on the final audit findings and may assess deficient severance tax payments, interest, and penalties. Wyo. Stat. Ann. § 39-14-208(b)(iv) (2009).

59. The Department's decision to assess additional severance taxes and interest rested on the DOA audit findings that Patriot's record keeping only identified a gas sale and purchase between Patriot and UET. In fact, without the testimony of Mr. Cree and Mr. Williams, the Board believes it would be difficult, if not impossible, to identify any separate financial agreement because the documents only appear to confirm gas sales and purchases with deductions for transportation and marketing costs. *Supra* ¶¶ 16-21, 25-28, 36-40, 45.

60. Patriot's record keeping provided no useful evidence, whatsoever, of a separate financial agreement, as opposed to a gas sale/purchase. Further, the internal spreadsheet identifying amounts due under the Hedge was not understandable without Mr. Cree's and Mr. Williams' testimony. Mr. Grenvik explained that "it is virtually unheard of not to have complete documentation[.]" (Tr. vol. II, 421). He testified that because of the record keeping, "all we have is -- is [Patriot's] word and UET's confirmation" that the hedge terms were as testified to by Mr. Cree and Mr. Williams. (Tr. vol. II, 435)(Tr. vol. I, 115, 435). *Supra* ¶¶ 16-21, 25-28, 36-40, 45.

61. The record keeping of the various transactions was so commingled, it was difficult to differentiate income from the gas sale/purchase, from the transportation, the marketing, or the Hedge income. (Tr. vol. I, 115). *Supra* ¶ 25.

62. Patriot did provide the auditors with the internal spreadsheet during the audit that purportedly identified the Hedge payment exchanges, but did little to explain the spreadsheet or the hedge accounting to the auditors. Mr. Grenvik explained that internal documentation like this spreadsheet is suspect because it is not subject to the give and take of negotiations that are then documented by the parties in a written contract. (Ex. 506). *Supra* ¶¶ 19, 26, 36.

63. In addition to recording the hedge accounting on documentation identical to that of a gas sale/purchase, Patriot also accounted for the hedge income in its corporate financial statements as a physical sale of gas, electing the normal purchase and sale exception under the accounting standards. Mr. Cree testified that Patriot's internal auditors initially believed the Hedge should be identified as a "separate financial hedging transaction," and not as a gas sale, but the company identified it as a gas sale, anyway, believing it would be easier for its investors to understand. (Tr. vol. I, 195) (Tr. vol. I, 195-97). *Supra* ¶¶ 27-28.

64. It is further undisputed that Patriot and UET had no written contract outlining the terms of the Hedge Agreement. Exhibit 706, which Patriot and UET relied upon to demonstrate the Hedge terms, was incomplete and inaccurate. Specifically, Exhibit 706

does not identify the IFERC first of month pricing as a “settlement price” against the fixed hedge price of \$9.38, and it incorrectly mentions a non-existent Base Contract dated October 24, 2007. It further references a WIC Medicine Bow meter location and a Cheyenne Hub price adjustment for similar unexplained reasons. (Ex. 706). *Supra* ¶¶ 16-21, 36-38. Nor is Exhibit 706 signed by a Patriot representative. Without Mr. Cree’s and Mr. Williams’ testimony, Patriot’s record keeping is incomprehensible. Even with their testimony, however, the evidence of a Hedge was convoluted and difficult to follow because the records combined the accounting for the various agreements, making it very difficult to parse out the various exchanges. *Supra* ¶ 61.

65. In a case involving similar record keeping issues, the State Board found:

A taxpayer, such as Triton, which maintains an inaccurate accounting system in violation of Wyoming’s mineral taxation code, cannot be permitted to benefit from such action by being allowed to treat all, or a portion, of its costs as indirect mining costs. If this were permitted it would allow any Wyoming mineral taxpayer to simply set up an accounting system with a single cost center and then later claim that it is incapable of allocating any of its costs to mining, processing or transportation. Such a system would punish taxpayers who abide by the law and maintain efficient and accurate accounting books and records in accordance with Wyo. Stat. 39-14-108(b)(vii), previously Wyo. Stat. 39-6-304(o).

Triton Coal Co., Docket No. 99-64 (August 30, 2000), 2000 WL 1419651, ¶109 (Wyo. St. Bd. Eq.).

66. Like *Triton Coal Co.*, Patriot completely failed to comply with the statutory requirement that it “keep accurate books and records of all production subject to severance taxes[.]” Wyo. Stat. Ann. § 39-14-208(b)(vii) (2009). The record keeping was so commingled as to make the gas sale/purchase indistinguishable from any separate financial transaction without verbal explanation of the terms and the accounting, in clear disregard of the statutory requirement that producers maintain accurate and sufficient records to allow verification of taxable value. *Supra* ¶¶ 16-21, 25-28, 36-40, 45, 58.

67. Addressing Patriot’s record keeping issues, the Department argues that the “terms and conditions of the Base Contract, Gas Purchase Agreement and the \$9.38 Confirmation are clear and unambiguous[.]” and should be considered without the benefit of testimony to explain the transactions. (Wyo. Dep’t of Revenue’s Closing Arg. 8). The Department argues the State Board may not consider Patriot’s evidence offered to change or extend the clear meaning of the language used in those agreements. It argues that the parole evidence rule prevents the State Board from relying on Patriot’s testimony that adds to or contradicts those documents. *Id.* Patriot responds that courts may consider evidence of the

surrounding circumstances to determine parties' intent in executing a contract or other document. (Pet'r Patriot Energy Resources LLC's Closing Arg. 13).

68. The Wyoming Supreme Court provided the following guidance regarding the parol evidence rule:

The parol evidence rule generally states that the intent of the parties to a contract or instrument is to be determined solely from the language of the instrument and extrinsic evidence may be examined only when the language is ambiguous. However, we depart from the parol evidence rule if the evidence is used to establish a separate and distinct contract, a condition precedent, fraud, mistake, or repudiation. Evidence of an oral agreement is considered if the oral agreement does not vary the terms of the writing, or if it is "separate and distinct from, and independent of, the written instrument." In other words, the parol evidence rule "does not affect a purely collateral contract distinct from, and independent of, the written agreement, even though it relates to the same general subject matter and grows out of the same transaction, if it is not inconsistent with the writing."

Belden v. Thorkildsen, 2007 WY 68, ¶ 16, 156 P.3d 320, 324-325 (Wyo. 2007) (citations omitted).

69. The State Board finds that Patriot's testimony was not inconsistent with the written documentation, and was instead offered to explain it. In fact, the testimony was absolutely essential to the State Board's understanding of the transactions and their relationships to each other and among the parties to the agreements. Moreover, Patriot used this testimony to establish a "separate and distinct" contract, which is not prohibited under the parol evidence rule. *Id.* Patriot also discussed the oral Hedge Agreement, which testimony did not "vary the terms" of Exhibit 706, instead more fully explaining it and the reasons for its use. *Id.* For these reasons, the State Board finds that it may appropriately consider Patriot's evidence relating to and explaining the exhibits offered in support of the Hedge Agreement.

70. The State Board must also consider Patriot's claim that a fundamental error in the audit requires reversal because the DOA did not consider Exhibit 506, the spreadsheet, in its audit. (Pet'r Patriot Energy Resources LLC's Closing Arg. 14-16). Explaining the DOA's disregard of the spreadsheet, Mr. Weekly testified that the auditors did not need to consider it because other documentation revealed the transaction confirmation terms, the invoices for payment, and the wire transfers or checks to "complete the circle." (Tr. vol. II, 290). *Supra* ¶¶ 32, 36. The State Board also notes that the spreadsheet certainly does not speak for itself, and Mr. Weekly indicated that Patriot did not explain the importance

of that document to the auditors during the audit, leaving the auditors to guess at its significance. *Supra* ¶¶ 36-39, 44-45.

71. The DOA did not fail to consider the document upon Patriot's request to do so. Instead, the DOA believed that other documents adequately tracked the exchanges, making the spreadsheet unnecessary. It was only through Mr. Cree's and Mr. William's testimony at hearing that the spreadsheet's relevance became apparent. The Board finds it somewhat disingenuous, given Patriot's failure to accurately and appropriately document the Hedge Agreement or to explain the spreadsheet during the audit, that Patriot argues that the "audit was fundamentally flawed" because the DOA did not simply accept the spreadsheet as necessary documentation and recognize its potential significance and meaning during the audit. (Pet'r Patriot Energy Resources LLC's Closing Arg. 2). *Supra* ¶¶ 36-39, 44-45.

72. The State Board finds that the audit was not "fundamentally flawed," nor did the DOA err in failing to consider the spreadsheet during the audit. Indeed, Patriot is singularly responsible for that lack of consideration given its own failure to maintain accurate and appropriate records or to offer an adequate explanation of the spreadsheet during the audit. *Supra* ¶¶ 36-39, 44-45.

73. Despite its lack of accurate record keeping, Patriot presented considerable testimony explaining and identifying a separate financial transaction. Although Patriot and UET agreed they had no written contract outlining the hedge terms, Mr. Cree's and Mr. Williams' testimony was consistent regarding the terms of the financial agreement, how it was documented, and how it was paid out between the parties. *Supra* ¶¶ 13-23. In fact, in its written Closing Argument, after hearing the explanations of the Hedge, the Department appeared to concede that the financial agreement between Patriot and UET existed, arguing instead that the Hedge Agreement was part of the integrated transaction between Patriot and UET. (Wyo. Dep't of Revenue's Closing Arg. 3-7).

74. Despite Patriot's failure to maintain accurate records, the State Board finds that Patriot presented sufficient credible evidence and testimony that on June 25, 2008, Patriot and UET entered into a financial agreement they called a Hedge Agreement that they confirmed on a standard sale/purchase transaction confirmation form. (Ex. 706).

2. Do the mineral valuation statutes authorize the Department to include the income Patriot realized from the Hedge Agreement with the "sales price" of its gas production for severance tax purposes?

75. Although the State Board finds that Patriot established it had a Hedge Agreement with UET, the State Board must also consider whether the Department could consider the income from the Hedge when it determined the total sales price UET paid for Patriot's gas.

76. The State Board must initially consider whether the relevant statutes are unambiguous and, if so, must consider the plain language of the statute to give effect to the intent of the legislature. *Exxon Mobil Corp.*, ¶ 11, 219 P.3d at 134, *supra* ¶ 53. However, in interpreting statutes, the State Board will give deference to the statutory interpretation of an agency charged with the administration of those statutes unless that interpretation is clearly erroneous. *Parker Land & Cattle Co.*, 845 P.2d at 1045, *supra* ¶ 54.

77. “To determine whether a statute is ambiguous, we are not limited to the words found in that single statutory provision, but may consider all parts of the statutes on the same subject.” *Exxon Mobil Corp.*, ¶ 11, 219 P.3d at 134. We must consider the ordinary and obvious meaning applied to these words as they are arranged in paragraphs, sentences, clauses and phrases to express intent. *Parker Land & Cattle Co.*, 845 P.2d at 1042, *supra* ¶ 54.

78. The Department correctly used the netback valuation method, which is defined as “the sales price minus expenses incurred by the producer for transporting produced minerals to the point of sale and third party processing fees.” Wyo. Stat. Ann. § 39-14-203(b)(vi)(C) (2009). *Supra* ¶¶ 31, 41.

79. “Sales price” is defined as “the transaction price determined in connection with a bona fide arm’s length sale[.]” Wyo. Stat. Ann. § 39-14-201(a)(i) (2009). A “[b]ona fide arm’s-length sale” is “a transaction in cash or terms equivalent to cash for specified property rights[.]” Wyo. Stat. Ann. § 39-14-201(a)(ii) (2009).

80. Considering the ordinary and obvious meanings of the relevant words and phrases in these statutes as they are arranged, the State Board finds that the above statutes are unambiguous, clearly identifying the Department’s obligations in establishing valuation. “Sales price” is the “transaction price” paid by the purchaser to the producer for the property, and “transaction price” is the overall exchange of value between the parties, as noted by the language defining a “bona fide arm’s-length sale” as “a transaction in cash or **terms equivalent to cash**[.]” Wyo. Stat. Ann. § 39-14-201(a)(i), (ii) (2009) (emphasis added). The legislature requires the Department to look at the “transaction price” or the overall exchange of value between the parties. *Supra* ¶¶ 34, 41.

81. Further, as Mr. Grenvik stated, the Department interprets this statute to mean the legislature intended the Department to determine “sales price” from the entirety of “transactions” between parties. *Supra* ¶ 41. He stated that “sales price refers to the transactions that are associated with the minerals being produced.” (Tr. vol. I, 424). *Supra* ¶ 34. The State Board gives deference to the Department’s interpretation of this statute as the agency charged with the administration of the statutes, *Parker Land & Cattle Co.*,

845 P.2d at 1045, *supra* ¶ 54, and finds it is not clearly erroneous.

82. The State Board agrees with the Department that the plain, ordinary and obvious meaning of the phrase “sales price,” considering its arrangement in this statute, requires the Department to consider all aspects of mineral industry business transactions for tax purposes.

83. This interpretation is further strengthened by the Wyoming Supreme Court’s finding that an earlier, very similar version of the mineral valuation statutes required that the Department consider all surrounding transactions to effectuate the legislative intent. *EOG Res., Inc., v. Dep’t of Revenue*, 2004 WY 35, ¶ 21, 86 P.3d 1280, 1286 (Wyo. 2004).

84. In *EOG Resources, Inc.*, EOG paid severance and ad valorem tax for severance of minerals as part of a financing arrangement known as a “volumetric production payment” (VPP) agreement. *Id* at 1282. The Department reviewed the several transactions comprising the VPP agreement and determined that an arm's length sale of minerals had occurred. It calculated a valuation based on contract pricing and assessed additional tax and interest. *Id* at 1283-85. The Board affirmed the Department's actions. EOG appealed on the basis that the entirety of the VPP agreement constituted a financing agreement warranting treatment as a non-arm's length sale. *Id* at 1283-84. In other words, it argued, as Patriot does in this case, that because the VPP was a completely separate financing arrangement that did not involve the production of gas, it should not be considered in the valuation assessment. The Supreme Court agreed with the Department and the State Board, finding:

Under the statute, valuation is determined by the type of transaction associated with the severance. § 39-2-208(c), (d). **By this language, the legislature has directed that the Department and the Board view this transaction in its entirety.** That review revealed that this transaction intended something beyond mere financing. A sale was intended based upon the “index pricing” referenced in the Exchange Agreement and the Department properly relied upon that index pricing as the parties’ valuation of the product’s fair market value. **Our review agrees with this assessment of the transaction and neither those entities nor this Court is permitted to ignore legislative intent because the contracting parties designated the transaction as a financing arrangement. Producing natural gas by means of complex financing, brokering, and sales agreements may well warrant different valuation treatment; however, the present statutory scheme does not permit it and changing that**

scheme is a matter for the legislature and beyond the purview of this Court.

EOG Res., Inc., v. Dep't of Revenue, 2004 WY 35, ¶ 21, 86 P.3d 1280, 1286 (Wyo. 2004) (emphasis added).

85. Although the agreement in the present case is of a different type and for a different purpose than that in the *EOG Resources, Inc.* case, the Supreme Court's reasoning applies similarly in that the legislature directed the Department to consider the entirety of the transactions. *Id.* To do otherwise would allow parties to artificially reduce their tax liability through these various types of side agreements.

86. Considering the transactions between Patriot and UET in their entirety to fully capture all consideration exchanged for Patriot's gas production, the State Board finds that Patriot's own evidence established that the Hedge Agreement was an integral part of the overall transactions between the parties. Mr. Cree testified that no other entity was willing to agree to a hedge because of Patriot's financial condition; Mr. Williams testified the only reason he agreed to a hedge was Patriot's gas production and Patriot's agreement to sell all of that production to UET through the Gas Purchase Agreement. Mr. Cree and Mr. Williams both unequivocally testified that UET would not have entered into the Hedge Agreement were it not for the Gas Purchase Agreement giving UET the right to purchase all of Patriot's gas, which it used as the only apparent collateral available for the Hedge. *Supra* ¶¶ 15, 23-24.

87. Although Patriot and UET both agreed that the Hedge Agreement did not require the production of any gas, Mr. Williams was clear that he only agreed to the Hedge because he was comfortable that Patriot would produce 3 to 4 times the volume of gas required for a cash offset in the event Patriot was required to pay UET under the Hedge. Patriot may not initially have needed to produce gas under the Hedge, but that gas production formed the basic consideration for the contract – without the ability to produce gas to provide the collateral necessary for the contract, the Hedge would never have happened. *Supra* ¶ 23.

88. The State Board cannot reconcile the fact that the Gas Purchase Agreement formed the sole consideration for the Hedge Agreement, with Patriot's position that the Department could not consider them together for taxation purposes. Because the Gas Purchase Agreement for all of Patriot's gas production formed the consideration for the Hedge Agreement with UET, and UET was the only entity willing to enter into such a Hedge, it is at least possible that Patriot's need for the Hedge factored into the Gas Purchase Agreement terms. Although the legislature may not have considered this specific type of financial arrangement in drafting the statute, it likely recognized that various agreements like this between the same parties could affect gas sales and valuation. The Wyoming Supreme Court effectively drew this same conclusion in affirming the Department's

obligation to view transactions between parties in their entirety. See *EOG Res., Inc.*, *supra*, ¶¶ 83-84.

89. Further, if the Department separately considered various transactions among the same parties, ignoring the connection between them, such would open the door to inappropriate reductions in taxable value through the various transactions.

90. The State Board finds that the legislature intended the Department to consider all transactions between parties to verify a producer's "sales price." By statute, because the Hedge was part of the overall transactions between the parties, the Department validly, accurately and correctly included income Patriot received from UET as a result of the financial transaction to determine the taxable value of the gas production exchanged between the parties.

91. Patriot failed to persuade the State Board by a preponderance of the evidence that the Department improperly valued its mineral production from July 1, 2007, through June 30, 2009, or that the Department's calculated value exceeded the fair market value of the product, as defined by Wyoming Statutes outlined above. *Supra* ¶35.

3. Did the Department correctly assess interest against Patriot?

92. The Department is required to add interest to all delinquent severance taxes on any mineral produced on or after January 1, 1994. Wyo. Stat. Ann. § 39-14-208(c)(iv) (2009). "Taxes are delinquent pursuant to paragraphs (iii) and (iv) of this subsection when a taxpayer or his agent knew or reasonably should have known that the total tax liability was not paid when due[.]" Wyo. Stat. Ann. § 39-14-208(c)(ii) (2009).

93. Since 2004, taxpayers have been on notice that the Department's interpretation of the statutes at issue in this case was correct. See *EOG Res., Inc.*, ¶ 21, 86 P.3d at 1286, *supra* ¶83-84. Moreover, "parties making an agreement are presumed to know the law and to contract with reference to the law." *Garwood v. Garwood*, 2008 WY 129, ¶ 21, 194 P.3d 319, 327 (Wyo. 2008) (citation omitted). As such, Patriot knew or should have known the Department would consider all of the parties' transactions in determining taxable value. This is, perhaps, especially true in this case where Patriot's own records commingled and jointly accounted for the transactions, even referring to the Hedge as a gas sale in its financial statements to investors. *Supra* ¶¶ 16-21, 25-28, 36-40, 45, 58. For these reasons, the Department correctly imposed interest on the delinquent severance tax assessment.

D. Conclusions:

94. Upon review of the above factual findings, and applying the legal standards of review the State Board must follow in compliance with state statute and Department rules, the State Board finds that although Patriot established a Hedge Agreement with UET, that evidence also established that the Hedge was part of the overall “sales price” and consideration exchanged for the gas production and sales between the parties. Thus, the Department did not err in including the income from the Hedge Agreement in assessing additional severance taxes against Patriot.

95. The State Board agrees with the Department that Patriot knew or should have known that taxes were due on the entirety of their transactions with UET. The plain language of the statute requires consideration of entire transactions between these parties, and the Wyoming Supreme Court has confirmed this interpretation in *EOG, Resources, Inc., supra* ¶ 83-84. Patriot knew, or should have known, that the entire transaction was subject to taxation, and the Department correctly assessed interest against Patriot.

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ORDER

IT IS THEREFORE HEREBY ORDERED the Department's assessment of \$229,896.60 in additional severance tax against Patriot is affirmed in all respects.

IT IS FURTHER ORDERED that the Department's assessment of \$79,824.00 in interest against Patriot for its failure to pay the full amount of taxes due is affirmed, as well.


Pursuant to Wyo. Stat. Ann. § 16-3-114 and Rule 12, Wyoming Rules of Appellate Procedure, any person aggrieved or adversely affected in fact by this decision may seek judicial review in the appropriate district court by filing a petition for review within 30 days of the date of this decision.

Dated this 28th day of August, 2015.

STATE BOARD OF EQUALIZATION



E. Jayne Mockler, Chairman




Martin L. Hardsocg, Vice Chairman



Robin Sessions Cooley, Board Member

ATTEST:



Jessica M. Brown, Executive Assistant

CERTIFICATE OF SERVICE

I hereby certify that on the 20th day of August, 2015, I served the foregoing **DECISION AND ORDER** by placing a true and correct copy thereof in the United States Mail, postage prepaid, and properly addressed to the following:

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