

BEFORE THE STATE BOARD OF EQUALIZATION

FOR THE STATE OF WYOMING

IN THE MATTER OF THE APPEAL OF)	
WPX ENERGY ROCKY MOUNTAIN, LLC)	Docket No. 2020-08
FROM A DECISION BY THE DEPARTMENT)	
OF REVENUE (Mineral Tax Division))	

FINDINGS OF FACT, CONCLUSIONS OF LAW, DECISION, AND ORDER¹

APPEARANCES

Walter F. Eggers, III, and Kasey J. Benish, Holland & Hart LLP, appeared on behalf of Petitioner WPX Energy Rocky Mountain LLC (Petitioner or WPX).

Karl D. Anderson and James Peters, Wyoming Attorney General’s Office, appeared on behalf of the Wyoming Department of Revenue (Department).

SUMMARY

[¶ 1] This appeal concerns the taxable value of natural gas production, in particular, the deductibility of a particular pipeline transportation cost when applying the “netback” valuation method. Wyo. Stat. Ann. § 39-14-203(b)(vi)(C) (2021). The Department disallowed deduction of firm pipeline transportation fees paid to move WPX’s gas to the point of arm’s length sale. The Department disallowed a deduction of firm pipeline transportation fees paid for months during which WPX did not transport gas on the pipeline in question. It also disallowed deduction of firm transportation expenses for eight months during which WPX’s gas shipped through the Bison pipeline. The Department conceded that WPX was entitled to deduct firm transportation fees for the eight months that WPX gas shipped on the Bison Pipeline, but only at the contract-based unit rate paid, rather than deduction of the entire transportation expense. The Department asks this Board to revisit its ruling addressing similar issues in *In re WPX Energy, Inc.*, 2017 WL 6276019, Doc. No. 2016-31 (Wyo. St. Bd. of Equalization, Dec. 1, 2017) (*WPXI*).

¹ Our detailed review of confidential contract language requires issuance of this decision in two forms, one with those discussions of confidential information removed, and a complete version issued only to the parties in this appeal. In the incomplete decision form, we have withheld paragraphs 43-46, part of 47, and 52-53, from public view.

[¶ 2] The Wyoming State Board of Equalization, Chairman E. Jayne Mockler, Vice-Chairman Martin L. Hardsocg, and Board Member David L. Delicath, held a contested case hearing and received proposed findings of fact and conclusions of law from the parties. The State Board **reverses** the Department’s audit assessment and **remands** it to the Department for adjustment as the Department requests.

JURISDICTION

[¶ 3] WPX timely appealed from the Department’s audit assessment, dated January 28, 2020, within 30 days. We have jurisdiction to hear its appeal. (WPX 0089-0100); Rules, Wyo. State Bd. of Equalization, ch. 2 § 5 (2021).

ISSUES

[¶ 4] WPX identified four issues:

- A. Are pipeline reservation fees and transportation service charges fundamental components of the charges WPX pays for the transportation of natural gas?
- B. Was the Department’s decision prohibiting deductions for one portion of transportation charges (charges for unutilized capacity), contrary to the facts of natural gas transportation?
- C. Are transportation costs incurred after the statutory point of valuation deductible under Wyoming’s natural gas tax valuation statutes and the interpretations of those statutes by this Board and the Wyoming Supreme Court?
- D. Are the Department’s and Wyoming Department of Audit’s decisions in this case contrary to this Board’s findings and conclusions in the 2017 *WYX* Opinion?

(WPX Issues of Fact & Law & Ex. Index, pp. 1-2).

[¶ 5] The Department identified two issues:

- A. Is the Department’s audit-based assessment correct, proper, and in accordance with law?
- B. Did the Department correctly reject WPX’s request to include unutilized demand charges as transportation deductions?

(Dep't' Issues of Fact & Law & Ex. Index, pp. 1-2).

[¶ 6] Given this dispute's history and complexity, we reframe the issues:

- 1) Was WPX entitled to deduct, as a transportation expense, a pipeline reservation fee (firm transportation expense) paid for months when neither it, nor its marketing affiliate, shipped WPX-produced gas on that pipeline?
- 2) Was WPX entitled to deduct the entire monthly reservation fee (firm transportation charge) paid to a pipeline when its marketing affiliate used only a portion of the reserved capacity?

FINDINGS OF FACT

Introduction

[¶ 7] We again consider how WPX was to calculate its “firm” transportation expense deductions when valuing its coal bed methane production for state mineral tax² purposes. Natural gas producers and/or shippers may opt for “firm transportation services”³ so that regardless of competing industry participants or other factors, their ability to ship up to a set quantity of gas each month is assured. For that assurance, a producer or shipper pays the full reservation fee regardless of whether it ships gas or not. *See infra* ¶¶ 13, 39. If a producer instead opts for “interruptible”⁴ pipeline transportation services at a lower cost, its ability to ship gas depends on whether there is pipeline capacity available. *See infra* ¶ 39.

[¶ 8] The particular questions before us are whether, or how, WPX could deduct the reservation/demand fee it paid to the Bison Pipeline when calculating the taxable value of its natural gas production for months during which it used little or none of the pipeline's capacity. The Department issued an audit assessment to WPX disallowing deduction of all

² Wyoming imposes a severance tax on the extraction of minerals, and counties levy an ad valorem tax on the same mineral production value, in lieu of a property tax on the associated land (lease) surface. *See* Wyo. Const., art. 15, §§ 3, 11, 19; Wyo. Stat. Ann. §§ 39-13-102(m) (2021) (Department to annually assess gross product of all mines at fair market value); 39-13-103(b)(iii)(A) (2021) (mineral production taxed at 100% of fair market value); 39-14-202(a)(i) (2021) (Department to annually assess severance tax on oil and gas production at fair market value, after completion of the “production process.”); *see also* Wyo. Stat. Ann. § 39-14-203(b) (2021).

³ The term “firm transportation” is codified in Federal Energy Regulatory Commission (FERC) regulations enacted pursuant to the Natural Gas Policy Act of 1978 (NGPA), and means: “that the service is not subject to a prior claim by another customer or another class of service and receives the same priority as any other class of firm service.” 18 C.F.R. § 284.7(a)(3).

⁴ “Interruptible transportation” under the NGPA means that “capacity used to provide the service is subject to a prior claim by another customer or another class of service and receives a lower priority than such other classes of service.” 18 C.F.R. § 284.9(a)(3).

Bison Pipeline transportation costs between January 1, 2013 and December 31, 2015. Consequently, the Department assessed a severance tax deficiency of \$2,629,015.92. (DOR Exs. 500-501; WPX Exs. 108-109; Tr. at 37-39, 45-47, 167). The Department conceded during the contested case hearing that it should have allowed WPX deduction of the Bison Pipeline “reservation” fee for eight months during which WPX’s gas passed through the Bison Pipeline, *but only at the contract unit rate, rather than in total*. (Tr. at 102-11, 148-49, 158-61); *infra* ¶¶ 18-19. During the hearing, the Department indicated that it would waive the assessment of interest. (Tr. at 108).

[¶ 9] We addressed a similar transportation deduction question when WPX appealed the Department’s rejection of amended mineral tax returns for WPX’s 2012 natural gas production. *In re WPX Energy, Inc.*, 2017 WL 6276019, Doc. No. 2016-31 (Wyo. St. Bd. of Equalization, Dec. 1, 2017) (*WPX I*). There, we held that WPX demonstrated entitlement to the full deduction of “firm” transportation pipeline fees, rather than the Department’s allowance of only a portion of the fees tied to a corresponding fraction of pipeline capacity utilized. *Id.* at ** 9-11, ¶¶ 37-47. Interpreting Wyoming Statutes section 39-14-203(b)(vi)(C) (2011), we concluded that the Department improperly rejected WPX’s amended returns seeking a refund of severance taxes paid. *Id.*

[¶ 10] Not surprisingly, WPX relies upon our earlier ruling in pressing its current appeal. The Department counters that the first appeal did not correctly, nor comprehensively, reveal the facts. The Department argues that the evidence in the present appeal more clearly illuminates the transportation fee’s substance and operation. (Tr. at 147-48, 172; Dep’t’s Prop. Find. of Fact and Concl. of Law, pp. 12-13).

[¶ 11] Yet, the overarching question remains unchanged: may WPX deduct the entire “firm” transportation fee paid for capacity in several pipelines, regardless of the volume of gas it transported? An issue not encountered in its first appeal: may WPX deduct the reservation charge incurred for months during which it transported *no gas* on the pipeline? (Tr. at 108-09); *supra* ¶¶ 6, 8.

Evidence presented⁵: the pipeline transportation fees in question and parties’ claims

[¶ 12] After extracting and gathering⁶ natural gas from its wells, WPX or its marketing affiliate, WPX Marketing, eventually transported the gas production through one of several

⁵ The parties agreed to include as evidence the entire hearing transcript from *WPX I*, including expert testimony describing the difference between firm and interruptible pipeline transportation services. (DOR Ex. 511).

⁶ “Gathering” is defined as the “transportation of . . . natural gas from multiple wells by separate and individual pipelines to a central point of accumulation, dehydration, compression, separation, heating and treating or storage.” Wyo. Stat. Ann. § 39-14-201(a)(ix) (2021). The parties do not dispute the point of

market pipelines. The parties discussed two pipelines in this appeal, the Fort Union Pipeline and the Bison Pipeline, through which WPX's gas moved from Wyoming's Powder River Basin to various markets for sale. (Tr. at 54-65, 134-35, 152; Confid. Tr. at 49-52, 115-32; Confid. DOR Exs. 508A – 509D; Confid. WPX Exs. 113-124); *infra* ¶¶ 43-53.

[¶ 13] Pursuant to multiyear transportation contracts with each pipeline, WPX Marketing acquired transportation services on a “firm” or “non-interruptible” basis. *See infra* ¶¶ 43-45, 51-52. For these firm transportation services, WPX marketing paid a “demand” charge or “reservation” rate each month. The reserved capacity on the pipelines ensured that WPX's production would ship regardless of competing demand. (WPX Ex. 111, 0103-107; DOR Exs. 506, 000031-69, 511, 000255-34, 000275-281, 000300-317; DOR Confid. Exs. 508A-509D; Tr. at 31-32, 73-75, 84-85, 96-98); *supra* ¶ 7; *infra* ¶¶ 43-53.

[¶ 14] WPX also paid a “commodity” charge; a pipeline charge tied to the units of gas shipped each month. Producers or shippers opting for “interruptible” pipeline transportation would pay only the commodity charge for gas delivered for transportation, but were not assured that capacity on the pipeline would be available. (Tr. at 95-96); *supra* ¶ 7.

[¶ 15] The Department and WPX agree that the gas in question did not ship down the Bison Pipeline during 24 months of the three-year audit period. (Tr. at 60, 133-135, 143-44; DOR Ex. 506). In only one of the eight months that WPX gas passed through the Bison Pipeline did WPX Marketing use its entire reserved capacity. *Id.* In September of 2015, WPX sold its Powder River Basin natural gas interests, including the 13 production properties under audit. (Tr. at 28-29, 70-71, 134).

[¶ 16] WPX, directing our attention to the outcome of its first appeal, restated its position that it properly deducted all pipeline transportation fees, including the entire demand charge paid for firm transportation during the audit period, regardless of the volumes of gas transported. Steve Rodich, WPX's Manager of State Tax and Royalty Reporting, testified that WPX was entitled to deduct all reservation charges, even charges paid during months when WPX marketing *transported no gas on a particular pipeline*. (Tr. 29-30, 54-62; *see also* Confid. Tr. 115-23).

[¶ 17] Mr. Rodich reasoned “it is a cost that we incur to have the ability to move our volumes to market. So regardless of where that volume goes, those costs incurred were

valuation, the physical point in the flow of natural gas production downstream after which *deductible* transportation and/or processing costs begin to accrue under the netback formula. *Id.*; (Tr. at 31); *See also Williams Prod. RMT Co. v. St. Dep't of Revenue*, 2005 WY 28, ¶¶ 13-14, 107 P.3d 179, 184, & App. A. ¶¶ 89-93 (Wyo. 2005) (detailed discussion of netback method and significance of activities upstream and downstream of the statutory point of valuation).

paid so that we could move our volumes to market.” (Tr. at 66; *see also* Tr. at 67-68). Mr. Rodich added that the demand charges in question were tied to the Powder River Basin region and were therefore deductible from WPX’s tax liabilities incurred in that region, rather than liabilities tied to or associated with specific gas placed in a particular pipeline. (Tr. at 82-83).

[¶ 18] Matthew Sachse, a Department employee who reviewed the audit findings and participated in the assessment decision, spoke for the Department. The Department’s core position, he explained, is that WPX could properly deduct only transportation costs tracking with the gas transported, at the rate per unit set in the transportation contracts. Citing Wyoming Statutes section 39-14-203(b)(vi)(C) (2021), the Department contends that a transportation deduction for tax purposes must directly effectuate physical passage of the sold gas production through the pipeline for which the fee was paid. (Tr. at 108-111, 135-37, 139-43, 160-61, 167-68; Confid. Tr. 115-32). As such, the Department disagrees that WPX could deduct reservation fees paid to a pipeline for months that no gas production shipped on the pipeline. *Id.* Likewise, the Department disagrees that WPX could claim a transportation based on region of production, irrespective of which pipeline services were actually used. *Id.*

[¶ 19] Mr. Sachse testified regarding several misunderstandings from *WPX I*. WPX did not enter the pipeline transportation arrangements in question, explained Mr. Sachse. Rather, a WPX marketing affiliate, WPX Marketing, shipped the gas pursuant to the transportation contracts it entered with Bison and Fort Union. (Tr. at 111-12, 140-42, 148-50, 161-64). This is significant, the Department contends, because WPX Marketing purchased and sold WPX’s produced gas as part of its separate marketing business, rather than as a producer of gas. It purchased or otherwise obtained gas, transported it, and sold it at optimal prices, consistent with its business model. (Tr. at 136-39, 161-64, 180-81). The Department argued that WPX Marketing’s business objectives, including its reason for acquiring pipeline transportation services for the prices set, extended beyond the scope of WPX’s gas production business. (Tr. at 161-64). WPX did not disagree, but responded that the pipeline transportation fees were “passed” 100% back from WPX Marketing to WPX. (Tr. at 185-86). The record does not contain agreements or communications between WPX and WPX Marketing. It also does not include details of how gas transferred between these two companies, or how pipeline transportation costs were allocated “back” to WPX’s production.

[¶ 20] Mr. Sachse noted that claiming the entire reservation fee as a deduction during the eight months that its gas passed down the Bison Pipeline could result in extraordinary deductions per unit of gas transported, effectively zeroing the production’s taxable value. Given the reservation fee, Mr. Sachse estimated a per unit transportation fee deduction of \$164 per MMBtu for one month during which very little gas was moved down the Bison

Pipeline.⁷ (Tr. 145-47). Mr. Sachse explained that a typical pipeline transportation deduction per MMBtu would range between fifty cents to a dollar and ten cents. *Id.*

CONCLUSIONS OF LAW

A. State Board's review function and burdens of proof

[¶ 21] “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) (2021). As the adjudicating body, the State Board “[d]ecide[s] 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[.]” Wyo. Stat. Ann. § 39-11-102.1(c)(iv) (2021).

[¶ 22] “[T]he burden of proof with respect to tax valuation is on the party asserting an improper valuation.” *Williams Prod. RMT Co. v. State Dep't of Revenue*, 2005 WY 28, ¶ 7, 107 P.3d 179, 183 (Wyo. 2005). 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 (2021). “Once the presumption is successfully overcome, the burden of going forward shifts to the DOR to defend its valuation.” *Colo. Interstate Gas Co. v. Wyo. Dep't of Revenue*, 2001 WY 34, ¶ 10, 20 P.3d 528, 531 (Wyo. 2001) (citing *Basin Elec. Power Coop., Inc. v. Dep't of Revenue*, 970 P.2d 841, 851 (Wyo. 1998)). The taxpayer “bears the ultimate burden of persuasion to prove by a preponderance of the evidence that the valuation was not derived in accordance with the required constitutional and statutory requirements for valuing state-assessed property.” *Id.*

[¶ 23] 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

⁷ An Mbtu is 1000 “British Thermal Units,” a measurement of energy content in a substance such as natural gas or oil. An MMBtu refers to one million British Thermal Units. See *EOG Res., Inc. v. Dep't of Revenue*, 2004 WY 35, ¶ 7, n. 2, 86 P.3d 1280, 1283 (Wyo. 2004); *Williams Prod. RMT Co. v. Wyo. Dep't of Revenue*, 2008 WY 155, ¶ 27, n. 4, 197 P.3d 1258, 1267 (Wyo. 2008).

(Wyo. 2011) (quoting *Judd v. State ex rel. Wyo. Workers' Safety & Comp. Div.*, 2010 WY 85, ¶ 31, 233 P.3d 956, 968 (Wyo. 2010)).

B. Applicable statutory and regulatory provisions

[¶ 24] As reported by WPX, the Department accepted application of the netback method for valuation of the natural gas at issue. *Supra* ¶ 1. The netback method applies as follows:

(b) Taxable event. The following shall apply:

...

(vi) In the event the crude oil, lease condensate or natural gas production as provided by paragraphs (iii) and (iv) of this subsection is not sold at or prior to the point of valuation by bona fide arms-length sale, or, except as otherwise provided, if the production is used without sale, the department shall identify the method it intends to apply under this paragraph to determine the fair market value The department shall determine the fair market value by application of one (1) of the following methods:

...

(C) Netback -- **The fair market value is the sales price minus expenses incurred by the producer for transporting produced minerals to the point of sale and third party processing fees.** The netback method shall not be utilized in determining the taxable value of natural gas which is processed by the producer of the natural gas;

Wyo. Stat. Ann. § 39-14-203(b)(vi)(C) (2021) (emphasis added). The present dispute concerns primarily the statutory language in bold.

C. Application of law to evidence presented

[¶ 25] We revisit the primary dispute in *WPXI*, and we encounter an additional question: whether WPX could deduct pipeline reservation charges when it transported no gas on a particular pipeline. *See supra* ¶¶ 6, 8, 11. Because each tax year's mineral tax liability stands on its own, preclusive doctrines such as *res judicata* or *collateral estoppel* do not prevent a taxpayer or the Department from reasserting a legal claim or position for

subsequent production years.⁸ The Department, not satisfied with the factual exposition in the first *WPX Energy* appeal addressing the taxable valuation of WPX's 2012 coal bed methane production, supplied additional information with which to consider pipeline reservation charges applicable to WPX's 2013-15 production. *Supra* ¶ 19.

[¶ 26] But first, we consider the new question presented, which concerns 24 of the 32 months in the audit period: was WPX entitled to deduct the Bison Pipeline reservation fee for months during which it did not use the pipeline in question?

*Deduction of pipeline fees WPX or its marketing affiliate paid to Bison
for months during which no WPX gas production shipped on the Bison Pipeline*

[¶ 27] Applied to value natural gas production, the statutory “netback” valuation method plainly states that transportation expenses are deductible. *Supra* ¶ 24. The statute unfortunately does not address the deductibility of expenses for different transportation forms, services, or contract arrangements, such as the pipeline reservation fee in question. The Department has not prescribed by rule how taxpayers are to deduct transportation expenses. Rather, it follows unwritten administrative practices, which sets the stage for the present litigation. We are tasked with interpreting the statutory term “transporting” in light of WPX's argument that it may deduct pipeline fees paid for months in which it *did not* actually transport its gas on a given pipeline.

[¶ 28] We consult the rules of statutory interpretation to interpret and apply the oil and gas taxation statutes. *See Amoco Prod. Co. v. Dep't of Revenue, St. of Wyo.*, 2004 WY 89, ¶ 34, 94 P.3d 430, 444 (Wyo. 2004) (Primary consideration when interpreting tax statutes is determining legislative intent). “We begin by construing the statutory language according to the ordinary and obvious meaning of the words at issue according to their arrangement and connection.” *Id. citing Lodberg v. State*, 2004 WY 48, ¶ 5, 88 P.3d 1045, 1048 (Wyo. 2004). “We construe the statute as a whole, giving effect to every word, clause, and sentence, and we construe all parts of the statute *in pari materia*.” *Travelocity.com LP v. Wyo. Dep't of Revenue*, 2014 WY 43, ¶ 19, 329 P.3d 131, 138-39 (Wyo. 2014) (*quoting Redco Const. v. Profile Prop., LLC*, 2012 WY 24, ¶ 26, 271 P.3d 415-16 (Wyo. 2012)).

[¶ 29] The term “transporting,” which we discussed in *WPXI*, does not assist in answering the first question. *See WPXI*, ** 8-9, ¶¶ 32-33. Rather, we must deconstruct the valuation

⁸ Each year, producers are required to report their severance and ad valorem tax liability to the Department, including the facts and circumstances material to their reports. In response, the Department verifies taxable value, issues severance tax assessments, and issues corresponding notices of valuation for the mineral production to the appropriate county assessor for levy of property taxes. *See Wyo. Stat. Ann.* §§ 39-13-103(a)(i), (b)(iii) (2021); 39-14-202(a)(ii)-(iii) (2021); 39-14-207(a) (2021); 39-14-208(a) (2021) (Reporting, valuation, and assessment procedures).

statutes as a whole to glean legislative intent. The operative mineral valuation statute, Wyoming Statutes section 39-14-203(b) (2021), summarizes a typical mineral production stream's movement from the wellhead, through the gathering process, and downstream through completion of the "production process," called the "point of valuation." *Id.*; see *supra* ¶ 24. The statute then identifies valuation method options applied at the point of valuation. *Id.*

[¶ 30] Whichever type of natural gas (i.e. methane, helium etc.), natural gas liquid (ethane, butane, pentane, propane, etc.), oil (sweet, sour, etc.), or byproduct (i.e. sulfur) is at issue, taxpayers must account for them individually from an extraction, gathering, processing, transportation, and sales standpoint. For example, the legislature defines "natural gas" as "all gases, both hydrocarbon and nonhydrocarbon, that occur naturally beneath the earth's crust and are produced from *an oil or gas well.*" Wyo. Stat. Ann. § 39-14-201(a)(xv) (2021) (emphasis added). The definition continues, "[f]or the purposes of taxation, the term natural gas includes products *separated for sale or distribution* during processing of *the natural gas stream*" *Id.* (emphasis added).

[¶ 31] This becomes clear when considering how the legislature defines various production and post-production activities and/or pieces of equipment, including "dehydrator," "separating," "sweetening," "gathering," and "processing." Wyo. Stat. Ann. § 39-14-201(a) (2021). For example, because "processing" of the mineral stream into its valuable components is central to the valuation calculus, the legislature defined the word with care:

"Processing" means any activity occurring beyond the inlet to a natural gas processing facility that changes the well stream's physical or chemical characteristics, enhances the marketability of the stream, or enhances the value of the separate components of the stream. Processing includes ...fractionation, absorption, adsorption, flashing, refrigeration, cryogenics, sweetening, dehydration within a processing facility, beneficiation, stabilizing, compression ... wellhead pressure regulation or the changing of pressures and temperatures in a reservoir) and separation which occurs within a processing facility.

Wyo. Stat. Ann. § 39-14-201(a)(xviii) (2021).

[¶ 32] These terms and activities are important to the valuation process because taxpayers must identify the costs paid for these activities as services, or account for the actual costs to operate equipment or perform these particular functions. Taxpayers must then properly characterize the costs and apply them when performing several of the valuation methodologies. See e.g. *See Williams Prod. RMT Co. v. St. Dep't of Revenue*, 2005 WY 28, ¶¶ 13-14, 107 P.3d 179, 184, & App. A. ¶¶ 89-93 (Wyo. 2005) (detailed discussion of netback analysis applied to coal bed methane production in Powder River Basin); *BP*

America Prod. Co. v. Dep't of Revenue, 2005 WY 60, 112 P.3d 2005 (Wyo. 2005) (Application of the “comparable value” method, which substitutes and deducts comparable transportation or processing fees charged under similar circumstances); *Exxon Mobil Corp. v. State of Wyo., Dep't of Revenue*, 2009 WY 139, 219 P.3d 128 (Wyo. 2009) (whether various complex processes were deductible as natural gas “processing” under the “proportionate profits” valuation method).

[¶ 33] The five valuation methods in subsection (b)(vi) of the valuation statute, of which the netback method is one, then require that the actual or comparable costs to transport or process natural gas downstream from the point of valuation be summed, categorized, possibly allocated, possibly used for comparison, and possibly deducted to arrive at the mineral’s value at the point of valuation. Wyo. Stat. Ann. § 39-14-203(b)(vi) (2021); *but see* Wyo. Stat. Ann. § 39-14-203(b)(v) (2021) (For gas sold at or prior to the point of valuation in arm’s length transaction, that transaction establishes the fair market value). When considered in *pari materia*, the valuation formula and associated statutes are **mineral product-centric**, and costs incurred must tie directly to the defined activities that enhanced the sold mineral’s taxable value, such as processing and transportation.

[¶ 34] Contrary to WPX’s argued construction, the valuation statutes do not envision a generic, universal deduction of costs, such as WPX’s claimed “cost to transport gas from Wyoming,” or a cost tied to production only by geographical region. *Supra* ¶¶ 16-19. Rather, the specific costs to process or transport a quantity of gas are set against the arm’s length price received for the unit of gas valued.⁹ *See Wyo. Dep't of Revenue v. Guthrie*, 2005 WY 79, ¶¶ 17-35, 115 P.3d 1086, 1095-98 (Wyo. 2005) (coal bed methane producer required to report detailed deduction information in support of reported taxable value, even if subsumed within third party transactions); *Amax Coal Co. v. Wyo. St. Bd. of Equalization*, 819 P.2d 825, 833-34 (Wyo. 1991) (consideration of how reclamation costs and black lung taxes were to be deducted in valuing coal). Wyoming tax law does not accommodate deduction of theoretical or contrived costs. *See e.g. Wyodak Res. Dev. Corp. v. Wyo. Dep't of Revenue*, 2017 WY 6, ¶¶ 44-51, 387 P.3d 735-36 (Wyo. 2017) (Rejecting coal producer’s argued hypothetical point of valuation and deductible costs). Had the legislature intended a more inclusive or nonspecific deduction, or had it intended a deduction of all expenses, it might have simply taxed the producer’s profit.

[¶ 35] Finally, as complicated as Wyoming taxation often becomes, the statutory words implicitly anticipate easy and efficient identification of the point of valuation and costs

⁹ Also compelling was Mr. Sachse’s distinguishing of costs that specifically improve the mineral product or add value after the point of valuation, sometimes referred to as “nontaxable” deductible costs. (*See* Tr. at 110-11, 137, 154-55). This phrasing, unfortunately, exists primarily as subtext in theoretical or policy explanations, usually before this Board or in Wyoming’s courts. But, it too is imperfect, can be argued to achieve a range of results, and is not, therefore, a precise benchmark of deductibility.

allowed or disallowed as part of the valuation calculus. *See supra* ¶ 24. Industry practices and unanticipated technological developments may render complex what would otherwise be simple. *See In re Matter of Appeal of Westmoreland Kemmerer, LLC*, 2018 WL 4205402, Doc. No. 2017-35 (Wyo. State Bd. of Equalization, Aug. 23, 2018) (how to classify coal production given new mining technique). But, we are hesitant to embrace any interpretation that unduly complicates or blurs what otherwise is straightforward.

[¶ 36] We reject WPX’s assertion that it may deduct reservation fee expenses paid, but not directly applied to move a particular quantity of gas on a given pipeline. For those months during which WPX Marketing incurred pipeline reservation fees to transport gas on the Bison or Fort Union Pipelines, but did not actually transport gas production on that pipeline, the Department correctly rejected the deductibility of those reservation charges.

*Deduction of pipeline fees WPX paid to Bison
for months during which less than the full pipeline capacity was used*

[¶ 37] The Department again disagrees that WPX may claim more than the minimal fractional deduction, but presents additional evidence about how the parties structured the pipeline transportation service and fees. WPX requests this Board reaffirm the legal conclusions drawn in its first appeal, while the Department essentially asks the Board to reconsider given the additional illuminating evidence.

[¶ 38] WPX again directs our attention to the expert testimony of Kris Terry, who testified on its behalf in the previous appeal. (WPX Ex. 111, WPX 0102-103; DOR Ex. 511, 000287-299). She was a consultant with decades of oil and gas industry experience, including experience with the negotiation and formation of gas pipeline transportation agreements. *Id.*

[¶ 39] Ms. Terry explained the difference between firm and interruptible pipeline transportation services and the benefits of firm transportation to a producer. She explained the difference between “demand” or “reservation” fees and charges for interruptible pipeline services. (DOR Ex. 511, DOR 000300-305, 000314-321, 000324-330; *see also* WPX Ex. 111, 0104-106); *see supra* ¶¶ 7, 13-14. She described the fee structure as a two-part mechanism intended to recover pipeline costs of construction and operation. (DOR Ex. 511, DOR 000301-302, 000309-310, 000312-314; *see also* WPX Ex. 111, 0104-106). She disagreed with the Department’s position that a producer incurred only the smallest incremental portion of the fee relative to the units shipped, rather than the entire fee paid to reserve transportation capacity. (DOR Ex. 511, DOR 000318-322). She opined that WPX paid the entire reservation charge to transport the gas, regardless of how much capacity WPX used. (DOR Ex. 511, 000335-336, 000339).

[¶ 40] Having deferred to WPX’s expert in the first appeal, *WPX I* at * 10, ¶ 39, the Department now disagrees and focuses our attention upon the pipeline service agreements between Bison or Fort Union and WPX Marketing and, particularly, the reservation fee’s structure. *Supra* ¶¶ 18-20. For the Bison Pipeline services, the Department notes that the fee is a per-unit rate of approximately \$0.56. *Supra* ¶ 18. The Department reasons that WPX may therefore deduct only the minimal fractional rate per unit times the units actually transported, rather than the entire reservation fee irrespective of gas volume transported. *Id.*

[¶ 41] The answer to WPX’s claim lies in the parties’ pipeline transportation agreements and requires that we carefully examine the bargained-for consideration paid for the transportation service. Given the plain meaning of “transporting,” the correct deduction is the precise cost to “transport” the audited production to the point of sale. *See WPX I*, ** 8-9, ¶¶ 31-36 (meaning of “transport” within statute); *Supra* ¶ 24. The question requires that we apply rules of contract interpretation.

The fundamental goal of contract interpretation is to determine the intent of the parties. *Whitney Holding Corp. v. Terry*, 2012 WY 21, ¶ 36, 270 P.3d 662, 673 (Wyo. 2012). The “language of the parties expressed in their contract must be given effect in accordance with the meaning which that language would convey to reasonable persons in the time and place of its use.” *Ultra Res., Inc. v. Hartman*, 2010 WY 36, ¶ 22, 226 P.3d 889, 905 (Wyo. 2010) (quoting *Moncrief v. Louisiana Land Exploration Co.*, 861 P.2d 516, 524 (Wyo. 1993)). This Court employs “common sense in interpreting contracts and ascribe[s] the words with a rational and reasonable intent.” *Id.*, ¶ 22, 226 P.3d at 905. “When the provisions in the contract are clear and unambiguous, the court looks only to the ‘four corners’ of the document in arriving at the intent of the parties.” *Claman v. Popp*, 2012 WY 92, ¶ 26, 279 P.3d 1003, 1013 (Wyo. 2012) (citations omitted). “In the absence of any ambiguity, the contract will be enforced according to its terms because no construction is appropriate.” *Id.* (citation omitted).

Wallop Canyon Ranch, LLC v. Goodwyn, 2015 WY 81, ¶ 35, 351 P.3d 943, 952-53 (Wyo. 2015).

[¶ 42] Careful examination of the confidential Bison and Fort Union transportation contracts with WPX Marketing, which drew little attention in the first hearing, reveals two very different types of transportation service arrangements. We consider each and determine whether the Department correctly disallowed deductions for transportation.

Bison Pipeline LLC Rate Schedule FT-1 Service Agreement

[¶ 43] Removed due to inclusion of confidential information.

[¶ 44] Removed due to inclusion of confidential information.

[¶ 45] Removed due to inclusion of confidential information.

[¶ 46] Removed due to inclusion of confidential information.

[¶ 47] Removed due to inclusion of confidential information. . . . We disagree that the legislature intended “transporting,” as applied in the statutory netback method, to include a marketing affiliate’s cost to fund a pipeline. We are guided by the legislature’s core directive: taxpayers may deduct the direct costs incurred to transport gas from one point to the next. *Supra* ¶ 24; *WPXI*, ** 8-9, ¶¶ 32-33. Nothing less, nothing more.

[¶ 48] In this vein, the Department aptly distinguishes WPX Marketing from its affiliate producer, WPX. *Supra* ¶ 19. WPX Marketing, as a market purchaser, shipper, and seller of natural gas, sought to exploit additional, lucrative natural gas markets. (*See* WPX Ex. 111, WPX 0105-106; DOR 000308-11, describing WPX Marketing’s deliberation on whether to invest in additional pipeline capacity to enable sale of Powder River Basin natural gas production across additional markets). We too struggle to equate WPX Marketing’s long-term pipeline investment expenditures with that of a producer’s focused objective of acquiring basic pipeline transportation services to move a unit of production from the field to the point of sale.

[¶ 49] How, then, should the Department have isolated and allowed deduction of just that portion of the firm transportation expense paid to transport the produced gas from the point of valuation to the point of sale? The record before us does not include a breakdown of costs subsumed within the Bison Agreement reservation charge. And, it appears that neither the Department nor Department of Audit received information isolating the costs to move the gas in question. Neither is there evidence of transactions between WPX and its affiliate, WPX Marketing. *Supra* ¶ 19. In the absence of such evidence, or a surrogate transportation expense such as a comparable arm’s length transportation fee paid by others, the Department’s selected method is likely the best indicator of the base transportation expense for the gas in question. *Supra* ¶ 18. The contractual per unit transportation fee may not precisely reflect the cost to move WPX’s gas to the point of sale, but it is the only evidence of the unbundled cost to transport gas beyond the point of valuation.

[¶ 50] For the audit period at issue, we shall affirm the Department’s reliance on the contractual per unit rate of approximately \$0.56 per MMBtu times the actual volume sold.

Fort Union Firm Gas Gathering Agreement

[¶ 51] WPX or WPX Marketing entered a Firm Gathering Agreement entered with Fort Union Gas Gathering, L.L.C. in March of 1999. (Confid. DOR Ex. 508-A, DOR 000071-91; Confid. WPX Exs. 118-121, WPX 0164-93; Confid. Tr. 128-29).

[¶ 52] Removed due to inclusion of confidential information.

[¶ 53] Removed due to inclusion of confidential information.

[¶ 54] We have carefully parsed and contrasted the two agreements to make clear the reason for our reconsideration of the outcome reached in *WPX I*. See *supra* ¶ 9. We continue to view reservation or demand fees to be wholly deductible to the extent parties pay them narrowly to *transport gas*, consistent with the legislature’s intended scope and usage of the word “transporting.” *Supra* ¶ 24. Therefore, when contractual arrangements encompass considerations, liabilities, or business endeavors well beyond a *producer’s* basic cost to transport natural gas from the field to a point of sale, as was the case with WPX Marketing’s investment in the Bison Pipeline, such fees are no longer fully deductible as transportation. If taxpayers or the Department are unable to distill down such reservation fees to isolate that part of the fee paid to transport the gas volumes in question, they should identify a different source for the deduction.

[¶ 55] In any case, we resist any interpretation wherein the statutory gas transportation deduction under the statutory netback method effectively subsidizes a producer’s or shipper’s business strategies or investments beyond narrow deduction of a basic cost to transport. Unfortunately, complex downstream transactions may not easily allow identification of subsumed transportation costs.¹⁰

CONCLUSION

[¶ 56] For months during which WPX gas did not ship on the Bison Pipeline, WPX was not entitled to deduct a reservation fee paid to the Bison Pipeline. For the eight months

¹⁰ Given the complexity of petroleum industry processing and transportation transactions, and dearth of statutory language addressing how these complex arrangements fit within the valuation formulae for mineral taxation, rulemaking would benefit the Department and taxpayers immensely. Given the ease with which activities may be re-characterized for tax purposes, we believe that administrative rules are preferable to adjudicated answers when responding to evolving industry practices. (Tr. at 142-43, 171-74); see e.g. *Williams Prod. RMT Co. v. State Dep’t of Revenue*, 2005 WY 28, ¶ 12, 107 P.3d 179, 184 (Wyo. 2005) (producer of new type of natural gas production process in early 2000’s asserted separators and dehydrators performed deductible processing functions after point of valuation); *EOG Res., Inc. v. Dep’t of Revenue*, 2004 WY 35, 86 P.3d 1280 (Wyo. 2004) (whether “volumetric production payments,” a complex financing/investment arrangement involving gas production at multiple locations, established taxable value of Wyoming natural gas production).

during which WPX gas shipped on the Bison Pipeline, WPX could deduct the contract unit reservation rate for each unit shipped.

ORDER

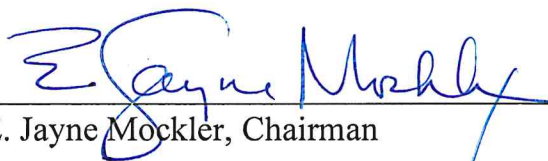
[¶ 57] **IT IS HEREBY ORDERED** that the Department of Revenue’s audit assessment is **reversed** and **remanded** to allow WPX a deduction of firm/uninterruptible pipeline transportation expenses limited to the contractual per-unit reservation rate that WPX, or its affiliate, paid the Bison Pipeline for months during which it shipped gas on that pipeline, to allow as a deduction the entire demand charge that WPX, or its affiliate, paid to the Fort Union Pipeline for months during which it shipped gas on that pipeline, and to remove the imposition of interest as requested.

[¶ 58] **IT IS FURTHER ORDERED** that WPX was not entitled to claim as a deduction firm transportation expenses paid to a pipeline for months during which neither it, nor its affiliate, shipped WPX’s gas production on that pipeline.


[¶ 59] **Pursuant to Wyoming Statutes section 16-3-114 (2021) 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 after the date of this decision.**

DATED this _____ day of September 2021.

STATE BOARD OF EQUALIZATION



E. Jayne Mockler, Chairman



Martin L. Hardsocg, Vice-Chairman



David L. Delicath, Board Member

ATTEST:

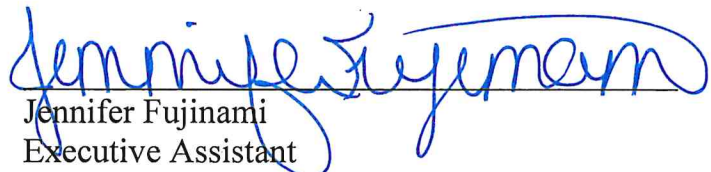

Jennifer Fujinami, Executive Assistant

CERTIFICATE OF SERVICE

I hereby certify that on the 13 day of September 2021, I served the foregoing **FINDINGS OF FACT, CONCLUSIONS OF LAW, DECISION, AND ORDER** by placing a true and correct copy thereof in the United States Mail, postage prepaid, and properly addressed to the following:

Walter F. Eggers, III, P.C.
Holland & Hart LLP
2515 Warren Avenue, Suite 450
Cheyenne, WY 82001

Karl D. Anderson
Senior Assistant Attorney General
James Peters
Assistant Attorney General
Kendrick Building
2320 Capitol Avenue
Cheyenne, WY 82002


Jennifer Fujinami
Executive Assistant
State Board of Equalization
P.O. Box 448
Cheyenne, WY 82003
Phone: (307) 777-6989
Fax: (307) 777-6363

cc: State Board of Equalization
Craig Grenvik, Mineral Tax Division, Dep't of Revenue
Department of Audit
ABA State and Local Tax Reporter