

ALABAMA TAX TRIBUNAL

SKLAR EXPLORATION COMPANY, §
LLC, §
Taxpayer, §
v. § DOCKET NO. MISC. 21-237-JP
STATE OF ALABAMA §
DEPARTMENT OF REVENUE

OPINION AND FINAL ORDER

The State of Alabama levies a privilege tax on those who produce or sever oil or gas from the state’s soil or waters or from beneath its soil or waters. Generally, the tax is 8% of the gross value of the oil or gas at the point of production, with certain exceptions. However, beginning May 1, 1985, the tax rate on the incremental production of oil or gas that results from certain enhanced recovery efforts is only 4% of gross value.

In 2019, Sklar Exploration Company, LLC (“Taxpayer”), petitioned the State Oil and Gas Board to approve a project in Escambia County that would qualify for the 4% tax rate. The Taxpayer also requested the Board to approve the amounts of oil and gas that could have been produced without the benefit of the project, so that the amounts of incremental production attributable to the project could be determined.

By order dated May 2, 2019, the Board granted the Taxpayer’s petition. The Taxpayer then petitioned the Alabama Department of Revenue for a refund of oil and gas privilege tax for the periods of December 2016 through May 2019, based on the difference between the rate at which the Taxpayer paid the tax and the reduced 4%

rate. The Revenue Department denied the petition for all periods prior to May 2019, because those periods preceded the Oil and Gas Board's approval date of the Taxpayer's enhanced recovery project. The Taxpayer appealed to the Alabama Tax Tribunal.

Question Presented

In a May 2019 order, Alabama's Oil and Gas Board approved the Taxpayer's project for periods prior to and including May 2019. And Alabama's appellate court previously had held that such an order entitled an oil and gas company to a refund of severance tax for periods prior to the date the order was entered. However, after the appellate decision, the Board adopted an administrative rule stating that action taken by the Board must be evidenced by an order "that shall then be effective as of that date unless ordered otherwise." Therefore, the question presented is whether the Board ordered an effective date that preceded May 2, 2019.

Facts

For purposes of this appeal, the parties stipulated to the following facts. (The exhibits referenced by the parties are not attached to this Opinion and Final Order.)

1. This is an appeal from the partial denial of a refund of oil and gas privilege taxes levied under Ala. Code §40-20-1, et seq.
2. Sklar Exploration Company, LLC (hereafter "Taxpayer") made a petition to the State Oil and Gas Board of Alabama (the "Board") requesting that the Board enter an order (i) approving the qualified enhanced recovery project for the Fishpond Oil Unit located in Escambia County, Alabama, and (ii) determining

the projected annual oil and gas production that could have otherwise been produced without the benefit of the initiation of said qualified enhanced recovery project, both as contemplated and authorized pursuant to the provisions of Section 40-20-1, et seq., Code of Alabama (1975). For all times material hereto, Taxpayer was the operator of the Fishpond Oil Unit. Beginning in November 2015, the Taxpayer began secondary recovery operations in the Fishpond Oil Unit by injecting gas into the reservoir for the purpose of increasing the ultimate recovery of hydrocarbons from the reservoir.

3. The petition was docketed by the Board as Docket No. 3-19-19-05.
4. The Board issued Notice of Meeting on the Taxpayer's petition for 10:00 a.m. on Tuesday, April 3 and Thursday, May 2, 2019, in the Board Room of the State Oil and Gas Board, Walter B. Jones Hall, University of Alabama Campus, 420 Hackberry Lane, Tuscaloosa, Alabama for consideration of the Taxpayer's claim.
5. A copy of the Notice of Meeting is attached hereto as Exhibit A.
6. At the scheduled Meeting of the Board, the Taxpayer presented the booklet of exhibits which is attached hereto as Exhibit B in support of its petition.
7. In accordance with standard practice before the Board, the Taxpayer's attorney prepared a proposed Order and sent it to the Board's attorney for approval.
8. On May 2, 2019 the Board entered Order No. 2019-22, a copy of which is attached hereto as Exhibit C.
9. The Taxpayer timely petitioned the Alabama Department of Revenue (the "Department") for a refund of oil and gas privilege tax under Ala. Code 40-20-1,

et seq. for the periods of December 2016 through May 2019. A copy of the petition (hereafter the “Refund Petition”) with the production schedules omitted is attached as Exhibit D.

10. The Department does not stipulate to any statement contained in or any part of Attachment A to the Refund Petition, except to stipulate that it was attached to the Refund Petition.
11. The Department performed an audit on the Refund Petition by examination of the records of Taxpayer in Shreveport, Louisiana to determine compliance with State of Alabama and oil and gas severance tax laws.
12. The Department determined that the Taxpayer’s Refund Request was calculated on the difference between the general rate paid and the special tax rate discount of Ala. Code §40-20-2(a)(2) for a certified enhanced recovery project for December 2016 through May 2019.
13. The Department denied the refund requested for periods prior to May 2, 2019, the date of the Order attached hereto as Exhibit C.
14. The Department made adjustments to the Taxpayer’s Refund Request for the month of May and recalculated and approved refunds for periods from May 2019 through March of 2020. The parties do not dispute the accuracy and validity of the refunds made for these periods.
15. A copy of the Department’s Audit Report without schedules is attached hereto as Exhibit E.

16. The Taxpayer disputes the legal and factual conclusions asserted by the Department in Exhibit E.
17. The Taxpayer and the Department agree to the calculation of the difference between the general rate paid and the special rate tax discount of Ala. Code §40-20-2(a)(2) for the periods of December 2016 through April 2019 in the Taxpayer's Refund Petition. The Taxpayer asserts that those amounts constitute overpayments of tax, while the Department disagrees that those amounts are overpayments of tax.
18. The Taxpayer appealed the partial denial of refund requested to the Alabama Tax Tribunal where it was assigned Docket No. MISC. 21-237-JP.
19. During the pendency of this appeal the Department contacted the Board and the Board responded by submitting a letter through its General Counsel. A copy of the letter and exhibits thereto are attached as Exhibit F.
20. The Taxpayer does not stipulate to any statement contained in Exhibit F but does stipulate with the Department to the authenticity of the attachments to the letter as copies of official governmental records of the Board.
21. A copy of Board Order 94-134 is attached hereto as Exhibit G, and the parties hereto stipulate as to the authenticity of this order as a copy of an official governmental record of the Board.
22. The stipulations made herein are made exclusively for the use and purposes of the Alabama Tax Tribunal in deciding the merits of this appeal and are not to be considered stipulations in regard to any other legal proceeding.

23. Further, the parties hereto stipulate not.

Law

The tax levy at issue reads as follows:

(a)(1) There is hereby levied, to be collected hereafter, as herein provided, annual privilege taxes upon every person engaging or continuing to engage within the State of Alabama in the business of producing or severing oil or gas, as defined herein, from the soil or the waters, or from beneath the soil or the waters, of the state for sale, transport, storage, profit, or for use. The amount of such tax shall be measured at the rate of eight percent of the gross value of the oil or gas at the point of production except as provided in subsequent subdivisions of this subsection. ...

(2) Effective May 1, 1985, and thereafter, the incremental oil or gas production produced during a given year resulting from a qualified enhanced recovery project shall be taxed at the rate of four percent of gross value at the point of production of the incremental oil or gas production. The State Oil and Gas Board of Alabama shall approve the qualified enhanced recovery project and the determination of the projected annual oil or gas production that could have otherwise been produced without the benefit of the initiation of the qualified enhanced recovery project at a hearing held pursuant to Section 9-17-7, as amended, and shall notify the Alabama Department of Revenue thereof.

Ala. Code § 40-20-2(a)(1) and (2).

And the phrase “qualified enhanced recovery project” is defined as follows:

A qualified enhanced recovery project shall mean an enhanced recovery project or supplemental enhanced recovery project that meets all of the following criteria:

- a. That the area where the enhanced recovery project or supplemental enhanced recovery project is employed has been unitized in accordance with the provisions of Article 3, Chapter 17 of Title 9, as amended.
- b. That injection of substances associated with the enhanced recovery project or supplemental enhanced recovery project has been or will be implemented as an integral part of the operations of the unitized area.

c. That the enhanced recovery project or supplemental enhanced recovery project be certified by the State Oil and Gas Board of Alabama as capable of incremental oil or gas production.

d. That the enhanced recovery project or supplemental enhanced recovery project be implemented on or after January 1, 1985.

Ala. Code § 40-20-1(22).

In 1996, Alabama's appellate court held that a taxpayer was entitled to a refund of oil and gas severance tax for periods prior to the date of an order entered by the Oil and Gas Board which approved the taxpayer's request for a reduced tax rate. *See State v. Union Oil Co. of California*, 686 So.2d 284 (Ala. Civ. App. 1996):

The State argues that Union Oil is not entitled to the refund on the ground that Union Oil was not eligible for the lower tax rate until August 24, 1994, the date of the Board's order certifying the project and approving the production numbers. In addition, the State argues that the Board's order does not specify that it applies retroactively and that the trial court was without authority to construe it as such. Furthermore, the State contends that the Board's order is ambiguous as to the starting date for the tax benefit, and that this ambiguity should be construed against Union Oil.

Union Oil contends that it is entitled to the refund because, it says, the Board's order clearly certifies the production amounts commencing on May 29, 1992. Union Oil argues that the order is not ambiguous in this respect. Union Oil further argues that the State misuses the term "retroactive." According to Union Oil, it is not asking that the order be retroactively applied.

...

We disagree with the State's argument that the Board's order is ambiguous as to the starting date for Union Oil's eligibility for the four percent tax rate. In its order, the Board clearly certified the oil and gas production amounts commencing on May 29, 1992, and notified the State of these amounts. Both parties to this appeal admit that attorneys for the Board and for Union Oil drafted the Board's order. If they had intended for Union Oil to be entitled to the four percent tax as of the date of the order, which was August 24, 1994, then they would have had no reason to

include in the order the projected oil and gas production amounts for the years 1992 and 1993. By entering the order, the Board was certifying that Union Oil was eligible for the lower rate beginning in May 1992.

...

In sum, the Board certified Union Oil's gas and oil production amounts from May 1992 through the expected duration of the project. It is in our opinion irrelevant in this instance that the order certifying the production amount was not entered until August 1994. Union Oil has met all of the requirements established in § 40-20-2 and is thus entitled to a four percent tax on its incremental oil and gas production beginning in May 1992.

State v. Union Oil Co., supra, pp. 286-87.

Four years after *Union Oil* was decided, the Oil and Gas Board adopted “Rules and Regulations Governing Practice and Procedure before the State Oil and Gas Board of Alabama.” See Ala. Admin. Code r. 400-7-1-.01, *et seq.* Concerning orders of the Board, the following rule was adopted:

During or after conclusion of any hearing, including continued sessions thereof, the Board shall promptly take such action as it may deem appropriate concerning the subject matter being considered by the Board, such action to be evidenced by oral order read or stated into the record granting, denying, continuing, amending, or other appropriate action regarding the petition or motion before the Board that shall then be effective as of that date unless ordered otherwise. Within a reasonable time thereafter, the Board shall enter a formal written order, executed by the appropriate members and attested by the Secretary of the Board, setting forth in extenso the action taken at such hearing upon each such petition or motion. A party may apply for rehearing before the Board under the procedures for rehearing established by the Alabama Administrative Procedure Act, Section 41-22-17, of the Code of Ala. 1975.

Ala. Admin. Code r. 400-7-1-.23

Analysis

Understandably, the Taxpayer relied upon *Union Oil* in arguing that it was entitled to the reduced rate for periods prior to May 2, 2019, which was the date of entry of the Board's order. As noted, however, the Oil and Gas Board's regulation, which was adopted after the *Union Oil* decision was issued, set the effective date of the Board's orders as the date that an order was entered, unless the Board ordered otherwise.

It is undisputed that the Board had the authority to adopt Rule 400-7-1-.23. *See* Ala. Code § 9-17-6(c), authorizing the Oil and Gas Board to make "such reasonable rules, regulations, and orders as may be necessary from time to time in the proper administration and enforcement of this article ..." And the order in question did not specify any other effective date than the date on which the order was entered, which was May 2, 2019. (There is no evidence before the Tax Tribunal that an oral order was read into the record during the Taxpayer's hearing before the Board, as directed by Rule 400-7-1-.23. Instead, the only order in the record is the written order of May 2, 2019, which was required by rule to set forth, "in extenso," the action taken by the Board at the hearing. *See* Black's Law Dictionary, Fifth Ed., p. 699, defining "in extenso" as "in extension; at full length; from beginning to end, leaving out nothing.") If the Board had intended for its order, which approved the Taxpayer's project and granted the Taxpayer a reduced tax rate, to be effective prior to May 2, 2019, the Board was required by law to order a different effective date. The Board did not do so.

Therefore, the Revenue Department's partial denial of the Taxpayer's refund request is upheld. Judgment is entered accordingly.

It is so ordered.

Entered February 14, 2023.

/s/ Jeff Patterson

JEFF PATTERSON

Chief Judge

Alabama Tax Tribunal

cc: Duane A. Graham, Esq.
David E. Avery, III, Esq.