

CLAY CALHOUN, SR. § STATE OF ALABAMA
Post Office Drawer 850108 DEPARTMENT OF REVENUE
New Orleans, Louisiana 70185-0108, ADMINISTRATIVE LAW DIVISION

Taxpayer, § DOCKET NO. MISC. 89-115

v. §

STATE OF ALABAMA §
DEPARTMENT OF REVENUE.

FINAL ORDER
ON APPLICATION FOR REHEARING

An Opinion and Preliminary Order was entered in this case on October 31, 1995. The Taxpayer applied for a rehearing, and the parties filed briefs and reply briefs in support of and in opposition to the rehearing.

The primary substantive issue in dispute involves the so-called "workback" method of valuing oil and gas at the wellhead.

The Alabama Supreme Court has ruled that the workback method can be used, but only if certain conditions are met. See, State v. Phillips Petroleum Co., 638 So.2d 893 (1994). The parties agree that the workback method may be used in this case. However, they disagree concerning how it should be computed. Specifically, should the Taxpayer's expenses relating to secondary flow meters, salt water disposal, depreciation, and transportation be allowed.

The Opinion and Preliminary Order held for the Department concerning the secondary flow meters, salt water disposal, and depreciation, but for the Taxpayer concerning the transportation expenses. Both sides objected.

Unfortunately, Alabama law does not address how the workback

method should be computed. The Revenue Department also has not promulgated any regulations discussing or defining the workback method. The only guideline for Alabama purposes is the broad definition set out by the Supreme Court in State v. Phillips Petroleum Co., 638 So.2d 886, 888 (Ala. 1992). However, that definition also does not specify which related or necessary but indirect processing and/or treatment costs should be allowed.

I have reviewed the Opinion and Preliminary Order and the arguments presented by both parties. While the Taxpayer presents a compelling argument, in my opinion, the Opinion and Preliminary Order is correct and must be upheld. The tax, as adjusted by the Department pursuant to the Opinion and Preliminary Order, is affirmed.

Concerning the penalties, Act 95-607 amended Code of Ala. 1975, §40-2A-11(h) so that the Administrative Law Division and Alabama's courts are now authorized to waive any penalty assessed under Title 40 for reasonable cause. See, Compaq Computer Corp. v. State, Admin. Law Docket F. 95-435, decided February 12, 1996. The penalties assessed by the Department under Title 40 are accordingly waived for reasonable cause. However, §40-2A-11(h) does not authorize the Administrative Law Division to waive the penalties assessed under Title 9, Code of Ala. 1975. The Title 9 penalties at §§9-17-28 and 9-19-29 were repealed by Act 92-186, effective October 1992. However, they were in effect during the subject

period. Consequently, those penalties must be affirmed.

I note that interest accumulated on the State assessment is \$35,196.32, versus a total tax liability of \$39,766.11, and that Baldwin County interest is \$4,326.84, versus a total tax due of \$4,811.96. Unfortunately, Alabama law does not provide or allow for a waiver or reduction of interest on taxes due.

The above considered, judgment is entered against the Taxpayer for State tax, interest, and penalty (Title 9 only) in the amount of \$79,297.12, and Baldwin County tax plus interest in the amount of \$9,138.80. Additional interest is also due from November 30, 1995.

This Final Order on Application for Rehearing may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §§40-2A-9(f) and (g).

Entered May 9, 1996.

BILL THOMPSON
Chief Administrative Law Judge