

**BEFORE THE BOARD OF TAX APPEALS
STATE OF KANSAS**

IN THE MATTER OF THE EQUALIZATION
APPEAL OF LARIO OIL & GAS COMPANY
FOR THE YEAR 2012 IN KINGMAN
COUNTY, KANSAS

Docket No. 2012-6058-EQ

ORDER

Now the above-captioned matter comes on for consideration and decision by the Board of Tax Appeals of the State of Kansas.

Lario Oil & Gas Co., Taxpayer, was represented by and through its counsel Bradley A. Stout of the Adams Jones Law Firm, P.A. Kingman County, Kansas (the "County") was represented by and through its counsel S. Eric Steinle of Martindell Swearer Shaffer Ridenour LLP.

The parties' *Joint Stipulation of Facts* was filed with the Court on December 20, 2013 and the Taxpayer's *Brief* was received on January 13, 2014. On March 6, 2014, Kingman County, Kansas (the "County") filed its *Response Brief* and on March 20, 2014, the Taxpayer filed its *Reply*. On July 8, 2014, the Board certified an *Order Staying Proceedings* in this matter pending a final decision in *In re Protest of Rakestraw Brothers, L.L.C.*, 337 P.3d 62 (Kan. App. 2014). which was then pending judicial review before the Kansas Court of Appeals. On December 1, 2014, the Board issued an *Order Lifting Stay of Proceedings* that noted that the Court of Appeals had issued its opinion in *Rakestraw* on October 17, 2014, and that the time for any post-decision motions had lapsed. The *Order Lifting Stay of Proceedings* further set this matter for a status conference on December 18, 2014, wherein the Parties notified the Board that this matter was fully submitted and ready for adjudication on the merits.

After considering all of the evidence and arguments presented, the Board finds and concludes as follows:

Jurisdiction/Subject Property

An equalization application has been filed with the Board pursuant to K.S.A. 2013 Supp. 79-1609. The 2012 tax year is in issue. The subject matter is as follows:

Personal property -- a 2006 Taylor pulling unit, located
in Kingman County, Kansas assigned PPID#
048-PP-04320 KINGMAN WAREHOUSE.

Issues Presented

The Taxpayer requests the subject property be granted an exemption from ad valorem taxation pursuant to K.S.A. 79-223. Taxpayer challenges the County's assessment of the mobile pulling unit as a "mineral leasehold interest" or as "other tangible personal property not otherwise described" rather than as "commercial and industrial machinery and equipment" under Art. 11, § 1 of the Kansas Constitution. Asserting the pulling unit is "commercial and industrial machinery and equipment" acquired after June 30, 2006, the Taxpayer asserts the property is tax exempt pursuant to K.S.A. 79-223. The County asserts the subject property does not satisfy the statutory requirements for exemption and, as such, the Taxpayer's request should be denied.

Findings of Fact

The parties' *Joint Stipulation of Facts*, which is fully adopted herein, indicates in pertinent part, as follows: Taxpayer is an oil and gas producer with headquarters in Wichita, Kansas. In addition to other oil and gas interests located throughout Kansas, Taxpayer operates 43 oil wells, 35 gas wells, and 6 saltwater disposal wells in south central Kansas. Although Taxpayer operates these wells, it does not own 100% of the working interest of any of these properties. The oil and gas interests are located in Kingman County and other south central Kansas counties.

In addition, and as part of its south central Kansas operations, Taxpayer owned and operated a warehouse in Murdock, Kingman County, Kansas, at which it stored equipment and machinery used in its south central Kansas operations.

On September 20, 2006, Taxpayer purchased a 2006 Taylor Pulling Unit. A pulling unit is a derrick or mast, and a system of pulleys, winches, and other tools mounted to a wheeled chassis to allow the unit to be transported. A pulling unit is used to install or remove tubing, sucker rods, downhole pumps and related items into or out of a cased wellbore to enable or improve the efficacy of an oil well. The pulling unit is not used in the day-to-day production of oil and gas at any specific lease. In calendar years 2010 through 2012, the subject property was used at 57 different wells on 46 different leases in Kansas counties. When not in use, the subject property is stored at Taxpayer's Murdock warehouse.

In the *Kansas Oil and Gas Guide* (herein "*Guide*"), pulling units are referred to as either workover units or well service units. Since 1965, the State of Kansas, Division of Property Valuation (herein "PVD") has classified and taxed workover units or well service units that are in use on an oil and gas lease as part of the mineral leasehold interest (subclass 2 of Class 2 of § 1, Article 11 of the Kansas Constitution). When not in use, workover or well service units are classified and taxed as "all other tangible personal property (subclass 6 of Class 2 of § 1, Article 11 of the Kansas Constitution.) Since 1965, the *Guide*, published under the authority of PVD, has instructed that workover or well service units are to be valued as part of the oil and gas leasehold interest as subclass 2 or subclass 6 itemized equipment.

Kingman County has never listed, classified, valued, assessed, or taxed pulling units (workover or well service units) as subclass 5 commercial and industrial machinery and equipment. The County classes these properties as either mineral leasehold (subclass 2) or other tangible personal property (subclass 6).

Taxpayer has not treated the pulling unit or any other similar piece of equipment and machinery as part of an oil or gas lease. Prior to 2006, Taxpayer reported such items as machinery and equipment for property tax purposes. After 2006, the Taxpayer treated these items as exempt and, as a result, the subject pulling unit was not listed on Taxpayer's rendition filed for tax years 2007 through 2012.

For the 2012 tax year, the Taxpayer filed a Kansas Personal Property Assessment form, which included the subject property listed on an attachment titled "vehicle listing". The County placed the property on the tax rolls for 2012, appraised the pulling unit at a market value of \$287,200, with an assessment rate of 30% of its value (subclass 2 and subclass 6 of Class 2 of § 1, Article 11 of the Kansas Constitution each have 30% assessment rates). The Taxpayer appealed this 2012 assessment to the Board.

Applicable Law and Court Conclusions

All property in this state which is not expressly exempt is taxable. See K.S.A. 79-101. Tax exemption statutes are to be construed strictly in favor of taxation and against exemption, and the burden of establishing exemption rests with the applicant. *In re Application of Central Kansas E.N.T. Associates, P.A.*, 275 Kan. 893, 897, 69 P.3d 595 (2003). Uniformity and fairness in property taxation depends as much on uniform application of exemptions as uniform application of assessments. See *Topeka Cemetery Ass'n v. Schnellbacher*, 218 Kan. 39, 43, 542 P.2d 278 (1975).

Taxpayer asserts the constitutional sub-classifications of tangible personal property are mutually exclusive and the subject pulling unit falls within the common understanding of “commercial and industrial machinery and equipment.” Taxpayer contends the relevant authority for resolving this issue is the Kansas Constitution, and not the *Guide* or the history of PVD’s practices in regard to specific types of property.

K.S.A. 79-223(b) exempts from taxation “[c]ommercial and industrial machinery and equipment acquired by qualified purchase or lease made or enter into after June 30, 2006, as a result of a bona fide transaction not consummated for the purpose of avoiding taxation.” Further, for purposes of the exemption, the statute specifically defines “commercial and industrial machinery and equipment” as “property classified for property tax purposes within subclass (5) of class 2 of § 1 of Article 11 of the constitution of the state of Kansas.” K.S.A. 79-223(d)(2).

In *In re Equalization Appeal of Wedge Log-Tech, LLC*, 48 Kan. App. 2d 804, 300 P. 3d 1105 (2013), the Kansas Court of Appeals had occasion to examine whether, under the current constitutional and statutory scheme in Kansas, certain wireline equipment was properly classified as “commercial and industrial machinery and equipment” thereby making the property exempt from ad valorem taxation pursuant to K.S.A. 79-233. As with the rules of statutory interpretations, the Court found that when construing constitutional provisions, “the primary duty of the court is to look to the intention of the makers and adopters of ... [a] provision. *Id.* at 812 (quoting *State ex rel. Six v. Kansas Lottery*, 286 Kan. 557, 562-62, 186 P.3d 183 (2008)). The Court ultimately concluded that “in interpreting and construing the constitutional amendment, ... [it] must examine the language used and consider it in connection with the general surrounding facts and circumstances that cause the amendment to be submitted.” *Id.* (Emphasis original) (quoting *In re Tax Exemption Application of Central Illinois Public Services Co.*, 276 Kan. 612, 621, 78 P. 3d 419 (2003)). Thus, following the Court’s analysis in *In re Equalization Appeal of Wedge Log-Tech, LLC*, an examination of the property classification scheme in class 2 of § 1 of Article 11 of the Kansas Constitution and pertinent evidence of how pulling units were classified under that scheme when K.S.A. 79-223 was enacted is in order.

Article 11, section 1(a) provides, in pertinent part, as follows:

Class 2 shall consist of tangible personal property. Such tangible personal property shall be further classified into six subclasses, shall be defined by law for the purpose of subclassification and assessed uniformly as to subclass at the following percentages of value:

- (1) Mobile homes used for residential purposes: 11 1/2%.
- (2) Mineral leasehold interests except oil leasehold interests the average daily production from which is five barrels or less, and natural gas leasehold interests the average daily production from which is 100 mcf or less, which shall be assessed at 25% : 30%.
- (3) Public utility tangible personal property including inventories thereof, except railroad personal property including inventories thereof, which shall be assessed at the average rate all other commercial and industrial property is assessed: 33%.
- (4) All categories of motor vehicles not defined and specifically valued and taxed pursuant to law enacted prior to January 1, 1985: 30%.
- (5) Commercial and industrial machinery and equipment which, if its economic life is seven years or more, shall be valued at its retail cost when new less seven-year straight-line depreciation, or which, if its economic life is less than seven years, shall be valued at its retail cost when new less straight-line depreciation over its economic life, except that, the value so obtained for such property, notwithstanding its economic life and as long as such property is being used, shall not be less than 20% of the retail cost when new of such property: 25%.
- (6) All other tangible personal property not otherwise specifically classified: 30%.

The Taxpayer's argument that the subclasses of tangible personal property in the Kansas Constitution are mutually exclusive is in error. As noted by this body in a prior K.S.A. 79-223 exemption decision, "subclass (5), identified generally as 'commercial and industrial machinery and equipment', is so broadly drawn that it could conceivably embrace tangible personal property within any of the five subclasses of class 2 property." *In re Tax Exemption Application of McPherson Drilling*, Docket No. 2009-56-TX, at p. 3.

Since 1965, PVD has classified pulling units as either subclass (2) (when in use) or subclass (6) property (when not in use), but never as subclass (5) property. Further, since 1965, the *Guide*, which refers to a pulling unit as a workover unit or a well service unit, has instructed that these properties are to be valued as part of the oil and gas leasehold interest as subclass (2) or subclass (6) itemized equipment.

PVD is authorized to “[d]evis[e] or prescribe guides, or both, for the valuation of personal property.” K.S.A. 75-5105a(b). PVD has general supervision over Kansas county appraisers. See K.S.A. 79-1401, 79-1402, and 79-1404. A county appraiser is required to follow the guidelines, policies, and procedures that PVD issues. See K.S.A. 79-1412a and 79-1456.

Further, the County has never listed, classified, valued, assessed, or taxed pulling units as subclass (5) property. The County has consistently classified the subject property, when rendered, as subclass (2) or (6) property both prior to and after the enactment of K.S.A. 79-223.

The Board contrasts the evidence presented herein with that found in *In re Wedge Log-Tech, LLC*, 48 Kan App. 2d at 804. In said matter, the Court of Appeals affirmed a decision from this tribunal granting tax exemption to the applicant’s wireline equipment pursuant to K.S.A. 79-223. The record of said matter indicated the County had, in tax years preceding the tax exemption request, listed, classified, valued, assessed, and taxed the wireline equipment at issue as subclass (5) commercial and industrial machinery and equipment. *Id.* at 806. Further, the wireline equipment at issue was never listed by PVD in the *Guide* as mineral leasehold equipment, as the County had so classified and assessed it for the year subsequent to the enactment of K.S.A. 79-223. *Id.* at 814. The Court of Appeals in *In re Wedge Log-Tech, LLC* ultimately concluded the wireline equipment was “commercial and industrial machinery and equipment” under Art. 11, § 1 of the Kansas Constitution and granted the exemption request.

The Taxpayer has the burden of proof herein and has failed to present compelling evidence or arguments that persuade the Board that the subject pulling unit is property classified for property tax purposes within subclass (5) of class 2 of § 1 of Article 11 of the Kansas Constitution. Therefore, the Board concludes that the subject property fails to satisfy the statutory requirements for tax exemption pursuant to K.S.A. 79-223.

IT IS THEREFORE ORDERED that, for the reason set forth herein, the Taxpayer’s request for ad valorem tax exemption is denied.

Any party who is aggrieved by this order may file a written petition for reconsideration with this Board as provided in K.S.A. 77-529, and amendments

thereto. *See* K.S.A. 74-2426(b), and amendments thereto. The written petition for reconsideration shall set forth specifically and in adequate detail the particular and specific respects in which it is alleged that the Board's order is unlawful, unreasonable, capricious, improper or unfair. Any petition for reconsideration shall be mailed to the Secretary of the Board of Tax Appeals. The written petition must be received by the Board within 15 days of the certification date of this order (allowing an additional three days for mailing pursuant to statute).

Rather than filing a petition for reconsideration, any aggrieved person has the right to appeal this order of the Board by filing a petition with the court of appeals or the district court pursuant to K.S.A. 74-2426(c)(4)(A), and amendments thereto. Any person choosing to petition for judicial review of this order must file the petition with the appropriate court within 30 days from the date of certification of this order. *See* K.S.A. 77-613(b) and (c) and K.S.A. 74-2426(c), and amendments thereto. Pursuant to K.S.A. 77-529(d), and amendments thereto, any party choosing to petition for judicial review of this order is hereby notified that the Secretary of the Board of Tax Appeals is to receive service of a copy of the petition for judicial review. Please note, however, that the Board would not be a party to any judicial review because the Board does not have the capacity or power to sue or be sued. *See* K.S.A. 74-2433(f), and amendments thereto.

Rather than filing a petition for reconsideration or appealing this order, any aggrieved party may request, within 14 days of receiving this order, a full and complete opinion be issued by the Board pursuant to K.S.A. 74-2426(a), and amendments thereto.

Unless an aggrieved party files a timely written request for a full and complete opinion or a timely petition for reconsideration as set forth herein, this order will be appealable by that party only by timely appeal to the district court or the court of appeals as set forth above.

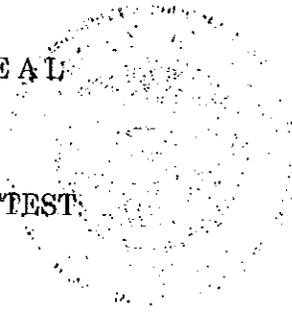
The address for the Secretary of the Board of Tax Appeals is Board of Tax Appeals, Eisenhower State Office Building, 700 SW Harrison St., Suite 1022, Topeka, KS 66603. A party filing any written request or petition shall also serve a complete copy of any written request or petition on all other parties. Please be advised that the administrative appeal process is governed by statutes enacted by the legislature and no further appeal will be available beyond the statutory time frames.

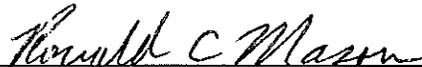
IT IS SO ORDERED

THE KANSAS BOARD OF TAX APPEALS

SEAL

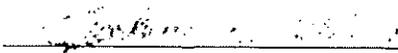
ATTEST




RONALD C. MASON, BOARD MEMBER


JAMES D. COOPER, BOARD MEMBER


ARLEN SIEGFREID, MEMBER PRO TEM


JOELENE R. ALLEN, SECRETARY

CERTIFICATION

I, Joeline R. Allen, Secretary of the Board of Tax Appeals of the State of Kansas, do hereby certify that a true and correct copy of this order in Docket No. 2012-6058-EQ and any attachments thereto, was placed in the United States Mail, on this 22nd day of

January, 2015, addressed to:

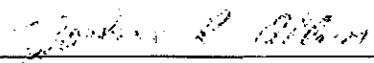
Michael T Hogan, Accounting Manager
Lario Oil and Gas Company
301 S Market St
Wichita, KS 67202

Bradley Stout, Attorney
Adams Jones Law Firm PA
1635 N Waterfront Pkwy, Ste 200
Wichita, KS 67206-6623

Richard Batchellor, County Appraiser
Kingman County Courthouse
130 N Spruce
Kingman, KS 67068

Eric Steinle, Attorney
Kingman County
Martindell Swearer Shaffer Ridenour LLP
PO Box 1907
Hutchinson, KS 67504-1907

IN TESTIMONY WHEREOF, I have hereunto subscribed my name at Topeka, Kansas.



Joeline R. Allen, Secretary