

Linda Willard

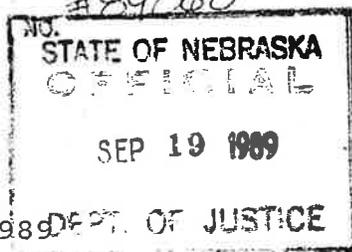
DEPARTMENT OF JUSTICE

STATE OF NEBRASKA

TELEPHONE 402/471-2682

STATE CAPITOL

LINCOLN, NEBRASKA 68509



ROBERT M. SPIRE
Attorney General
A. EUGENE CRUMP
Deputy Attorney General

DATE: September 18, 1989

SUBJECT: Valuation and Taxation of Mineral Interests.

REQUESTED BY: John M. Boehm, State Tax Commissioner

WRITTEN BY: Robert M. Spire, Attorney General
L. Jay Bartel, Assistant Attorney General

You have requested our opinion on several questions pertaining to the valuation and taxation of mineral interests. Your initial question relates to the manner of valuing mineral interests for property tax purposes. In this regard, you state that a method of valuing producing mineral interests has been proposed which is based on the prior year's average sale price per unit multiplied by the total units sold, without regard to the value of the recoverable reserve. Your specific question concerns whether the proposed use of prior year's production as a method of valuing producing mineral interests would violate any Nebraska constitutional or statutory provisions relating to the valuation of property for tax purposes.

Article VIII, Section 1, of the Nebraska Constitution, provides, in part: "The necessary revenue of the state and its governmental subdivisions shall be raised by taxation in such manner as the Legislature may direct. Taxes shall be levied by valuation uniformly and proportionately upon all tangible property and franchises," This provision of the Constitution requires that taxes upon all tangible property subject to taxation shall be levied by valuation, uniformly and proportionately. Lincoln Tel. and Tel. Co. v. County Board of Equalization, 209 Neb. 465, 308 N.W.2d 515 (1981). The uniform standard of value which the Legislature has established for purposes of valuing property for assessment in Nebraska is "actual value", which is defined in

Neb.Rev.Stat. §77-112(1) (Reissue 1986) as follows:

. . . actual value of property for taxation shall mean and include the value of property for taxation that is ascertained by using the following formula where applicable: (a) Earning capacity of the property; (b) relative location; (c) desirability and functional use; (d) reproduction cost less depreciation; (e) comparison with other properties of known or recognized value; (f)

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John Boehm
September 18, 1989
Page -2-

market value in the ordinary course of trade; and (f) existing zoning of the property.

For purposes of taxation, the terms "actual value", "market value", and "fair market value" mean exactly the same thing. Xerox Corp. v. Karnes, 217 Neb. 728, 350 N.W.2d 566 (1984).

Pursuant to Neb.Rev.Stat. §77-201 (Reissue 1986), ". . . all tangible property and real property in this state, not expressly exempt therefrom, shall be subject to taxation and shall be valued at its actual value." Neb.Rev.Stat. §77-103 (Reissue 1986) provides that "[t]he terms real property, real estate and lands shall include . . . mines, minerals, quarries, mineral springs and wells, oil and gas wells, [and] overriding royalty interests and production payments with respect to oil and gas leases," Consistent with this definition, the Nebraska Supreme Court has on several occasions recognized mineral interests as real property. State ex rel. Svoboda v. Weiler, 205 Neb. 799, 290 N.W.2d 456 (1980); Fawn Lake Ranch Co. v. Cumbow, 102 Neb. 288, 167 N.W. 75 (1918); see also Conway v. County of Adams, 172 Neb. 94, 108 N.W.2d 637 (1961). In light of the foregoing, the answer to your first question depends on whether the use of a valuation methodology for producing mineral interests based upon the prior year's production is consistent with the requirement that property be valued at its "actual value", in order to comply with the constitutional mandate of Article VIII, Section 1, that all tangible property shall be taxed "by valuation uniformly and proportionately".

A number of Texas cases reveal that, in the area of valuation of interests in oil and gas for ad valorem tax purposes, the value of lease and royalty interests is determined by multiplying the respective shares of the lessee and royalty owner in the average production of oil in barrels by different and variable multiples in dollars. Phillips Petroleum Co. v. Townsend, 63 F.2d 293 (5th Cir. 1933); Richardson v. State, 53 S.W.2d 508 (Tex.Ct.Civ.App. 1932), aff'd State v. Richardson, 126 Tex. 1, 84 S.W.2d 1076 (1935). The multiples used to arrive at such valuations are varied to allow for adjustments based on such factors as the changing price of oil, the cost of production, and estimated life of the wells. The basis for this method of valuation appears to rest upon the theory that the value of lease and royalty interests for purposes of purchase and sale is estimated in this manner. Phillips Petroleum Co. v. Townsend, supra, 63 F.2d at 295. See generally 4 Summers, Oil and Gas, c.26, §799 (1962).

In Blackmore v. P. & G. Oil and Gas Co., 52 Ohio App. 430, 3 N.E.2d 924 (1935), the Court of Appeals of Ohio held the taxation of a gas lessee's interest for ad valorem tax purposes at a value arrived at solely by the multiplication of the average daily production by \$60 per 1,000 cubic feet was erroneous and contrary

to law. In reaching this conclusion, the court noted that, while average daily production is a proper and necessary factor to consider in valuing an interest of this nature, numerous other factors must also be considered in determining the true value of a gas well, including: (1) the rock pressure of the well; (2) pipeline pressure in the immediate vicinity; and (3) the depth and condition of the well. Id. at _____, 3 N.E.2d at 926.

An examination of these decisions reveals that both Texas and Ohio have provisions in their state constitutions requiring uniform taxation of property in proportion to its value, wherein "value" refers to "reasonable cash market value" or "true value in money". Phillips Petroleum Co. v. Townsend, supra, 63 F.2d at 294; Blackmore v. P. & G. Oil and Gas Co., supra, 52 Ohio App. at _____, 3 N.E.2d at 926. This is very similar to the situation in Nebraska, wherein the Constitution requires that taxes on tangible property be levied by valuation uniformly and proportionately, and the Legislature, by statute, has established that "actual value" shall be the standard by which such uniformity is to be achieved. Neb. Const., art. VIII, §1; Neb.Rev.Stat. §§77-112 and 77-201 (Reissue 1986). Consistent with the decisions in Phillips Petroleum Co. v. Townsend, supra, and Blackmore v. P. & G. Oil and Gas Co., supra, we believe that consideration of prior year's production in the valuation of producing mineral interests for ad valorem tax purposes is not inconsistent with or contrary to Nebraska constitutional or statutory requirements. While production may appropriately be considered in the valuation process, however, the above-cited cases illustrate that a value based on production alone will not equate with the actual or market value of the interest. Accordingly, it is our opinion that, while consideration may be given to prior year's production in establishing the actual value of producing mineral interests, this factor alone should not be deemed exclusive in establishing such value for property tax purposes. Production may, however, be considered in connection with other appropriate factors or elements of value in determining the valuation of such interests.

Your second question concerns whether county assessors are required to record and value for ad valorem property taxation all mineral interests within the county, or whether assessors are only required to record and value mineral interests in situations where an application is filed with the assessor to place a severed mineral interest on the tax list in the county pursuant to Neb.Rev.Stat. §57-236 (Reissue 1988).

As noted previously, Neb.Rev.Stat. §77-201 (Reissue 1986) provides that ". . . all tangible property and real property in this state, not expressly exempt therefrom, shall be subject to taxation and shall be valued at its actual value." Furthermore, the terms "real property, real estate and lands" are defined to

include ". . . mines, minerals, quarries, mineral springs and wells, oil and gas wells, [and] overriding royalty interests and production payments with respect to oil or gas leases," Neb.Rev.Stat. §77-103 (Reissue 1986). Thus, as it is clear that mineral interests constitute real property subject to ad valorem taxation in Nebraska, such interests should be valued and assessed in the same manner as other real property, as required by Neb.Rev.Stat. §77-1301 et seq. (Reissue 1986). In our view, section 57-236 merely provides a statutory mechanism whereby the owner of the surface estate from which a mineral interest has been severed, or the owner of the mineral interest, may apply to the county assessor to have such severed mineral interest placed separately on the tax list of the county. This provision, enacted in 1981, was apparently adopted to codify the right of the owner of the surface estate to compel the county assessor to separately list a severed mineral interest in the name of the owner of such interest, recognized by the court in State ex rel. Svoboda v. Weiler, 205 Neb. 799, 290 N.W.2d 456 (1980). See 1981 Neb. Laws, LB 59. We do not, however, view the enactment of §57-236 as altering the general duty of the county assessor, which is to assess and list the value of all taxable property in the county, including mineral interests.

In a related question, you ask us to clarify the duties and obligations of county assessors with regard to determination of the ownership of mineral interests for purposes of assessment. In addition to the general duties of county assessors with regard to the assessment of real and personal property, we note that, pursuant to Neb.Rev.Stat. §77-1311 (Reissue 1986), certain specific duties as to the assessment of "producing mineral leases" are imposed on county assessors. Specifically, §77-1311 provides, in part:

It shall be the duty of the county assessor to examine the records in the office of the register of deeds and county clerk for the purpose of ascertaining whether mortgages on real estate and security interests on personal property, producing mineral leases, title notes, contracts, and bills of sale, intended to operate as a lien in the county, have been fully and correctly listed. He or she shall add to the assessment roll all omitted mortgages, security interests, producing mineral leases, title notes, contracts, and bills of sale intended to operate as a lien and belonging to residents of his or her county, and not otherwise assessed, upon notice to the owner thereof or his or her agents.

Pursuant to this provision, it is evident that the county assessor is required to annually review the records of the register of deeds and the county clerk to enable the assessor to add to the assessment roll the value of any producing mineral leases revealed

John Boehm
September 18, 1989
Page -5-

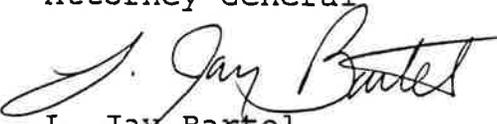
by such review, upon notice to the owner thereof or his or her agent. Apart from this specific statutory directive, we can provide no further guidance in regard to the statutory duties imposed on county assessors in relation to the assessment of mineral interests.

Finally, you have asked us to consider whether various types of machinery and equipment utilized in the extraction or production of mineral interests (such as casing, sucker rods, pump rods, electrical pumps, and other miscellaneous equipment) should be subjected to property taxation.

Again, as was previously noted, Neb.Rev.Stat. §77-201 (Reissue 1986) provides that ". . . all tangible property and real property in this state, not expressly exempt therefrom, shall be subject to taxation and shall be valued at its actual value" See Neb. Const., art. VIII, §2. While various types of personal property are exempted pursuant to Neb.Rev.Stat. §77-202 (Cum Supp. 1988), it does not appear that the type of property described in your letter would likely qualify for exemption under §77-202. In the absence of any constitutional or statutory provision establishing an exemption for such property, it must be valued and assessed for property tax purposes under Nebraska law.

Very truly yours,

ROBERT M. SPIRE
Attorney General



L. Jay Bartel
Assistant Attorney General

Approved:



Attorney General