

# THE KANSAS AD VALOREM TAX REFUND

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HEARING  
BEFORE THE  
SUBCOMMITTEE ON ENERGY AND POWER  
OF THE  
COMMITTEE ON COMMERCE  
HOUSE OF REPRESENTATIVES  
ONE HUNDRED SIXTH CONGRESS  
FIRST SESSION

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JUNE 8, 1999  
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**Serial No. 106-38**

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## THE KANSAS AD VALOREM TAX REFUND

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TUESDAY, JUNE 8, 1999

HOUSE OF REPRESENTATIVES,  
COMMITTEE ON COMMERCE,  
SUBCOMMITTEE ON ENERGY AND POWER,  
*Washington, DC.*

The subcommittee met, pursuant to notice, at 10 a.m., in room 2322, Rayburn House Office Building, Hon. Joe Barton (chairman) presiding.

Members present: Representatives Barton, Largent, Rogan, Shimkus, Wilson, Shadegg, Pickering, Fossella, Bryant, Hall, and McCarthy.

Staff present: Cathy Van Way, majority counsel; Jeff Krilla, professional staff member; and Sue Sheridan, minority counsel.

Mr. LARGENT [presiding]. We will call the meeting to order.

The chairman, Mr. Barton, is on his way over, but we wanted to get started in deference to everybody's schedule.

Today's hearing is on the Kansas ad valorem tax refund issue, and we are going to allow our panelists to speak on this. And I would like to defer to the ranking member, Mr. Hall, for his opening statement.

Mr. HALL. Thank you, Mr. Chairman and members of the committee.

The issues that are before us today only prove once again the old adage, justice delayed is justice denied, is very true. There aren't any good answers to this dilemma, and I think all parties probably realize that.

I thank you for having this hearing. I have some familiarity with the situation that exists here today.

The Hawkins oil field in east Texas is entirely within my district. In the 1980's the royalty owners were asked to refund hundreds of millions of dollars as a result of a determination by the Federal Government that the operator had charged too much for production in the Hawkins field during the time oil was under price controls.

The result was an absolute financial catastrophe for a number of royalty owners, people who had no knowledge of what price was being charged and had no way to protect themselves even if they did. The producer really had no choice but to pursue collection of amounts they had paid to the royalty owners because failure to do so would have left the company vulnerable to stockholders' suits. It was just a sorry situation all the way around.

The circumstances before us today are really very familiar. My sense is that the real villain is here is FERC, who appears to be

the biggest contributor to the delay and has exacerbated this situation, in my opinion. But there is enough blame to go around.

So after we hear the testimony, I think this committee is going to have some real decisions to make. What I hope ultimately will result is some forbearance on the parts of all parties. Yes, under the law these gas customers are entitled to recover the amount that they were overcharged, plus interest; however, those provisions were enacted to recover reasonable interest amounts over reasonable periods of time, in a matter of months, not 15 years or so.

The inequities to royalty and working interest owners that results from letting the interest toll and for the delay in informing these owners of the extent of their liability are really enormous. So all parties, including the Congress, are faced with trying to determine what is the best course of action to take. Unfortunately, we can only select from a lousy set of options.

I will listen very carefully to the testimony here today to see what remedies may be available and what might be done to prevent situations like this from arising to the future.

Mr. Chairman, I thank you. I yield back the balance of my time.

Mr. LARGENT. Thank you, Mr. Hall.

At this time, the Chair recognizes the gentleman from Tennessee for an opening statement.

Mr. BRYANT. Thank you, Mr. Chairman. I do want to welcome my colleague from the First District in Kansas and certainly acknowledge his interest in this legislation and his what I believe incredible amount of work on this. I look forward to hearing not only his testimony, but the other panels that are here today and yield back my time.

Mr. LARGENT. And the Chair recognizes the gentleman from Illinois for an opening statement.

Mr. SHIMKUS. Thank you, Mr. Chairman.

I, too, want to welcome my colleague from Kansas who is a strong advocate on this issue and has been working us over on it early and often. So I am looking forward to learning about it and following the procedures. Welcome, Jerry.

And I yield back my time.

Mr. BARTON. Has the gentleman from Texas given his opening statement?

Mr. HALL. I would like unanimous consent to insert the Honorable John Dingell's statement into the record.

Mr. BARTON. Without objection.

[The prepared statement of Hon. John D. Dingell follows:]

PREPARED STATEMENT OF HON. JOHN D. DINGELL, A REPRESENTATIVE IN CONGRESS  
FROM THE STATE OF MICHIGAN

Mr. Chairman, today's hearing explores issues relating to the treatment of the Kansas ad valorem tax on natural gas and its disposition under federal law: specifically the Natural Gas Act and the Natural Gas Policy Act.

There is a long and complex history behind this issue, which I am sure we will have recounted today by our esteemed witnesses. I will only point out that Federal Energy Regulatory Commission (FERC) has ordered that the costs of the Kansas tax be refunded to gas consumers and that in 1997, the D.C. Circuit held that since refund claims had been pending from 1983 forward, that FERC should order refunds with interest from 1983 forward.

Now, on March 18th of this year, Senator Roberts of Kansas succeeded in attaching language to the Supplemental Appropriations bill to exempt producers from having to pay interest on the refunds of the Kansas ad valorem tax. This is a very nice deal if you can get it, and it's certainly one that the IRS would never give you or me if we failed to pay our taxes for five years or more. However, Senator Roberts convinced his colleagues that this was a good idea and it passed the Senate along with the rest of the Supplemental bill. Noting that the House-passed bill contained no such provision, Chairman Bliley and I both conveyed our opposition to the Roberts language to the Appropriations Committee on the grounds that the provision was amending the Natural Gas Policy Act, a statute primarily within the jurisdiction of this Committee. Fortunately, the House position carried the day and the Roberts language was dropped in conference.

But jurisdiction was not the only reason I objected to the Roberts amendment. I also opposed this language because it clearly represented a transfer of wealth from my state to gas producers in the State of Kansas. I know my esteemed colleague from Kansas is concerned about whether the refunded money would ultimately find its way into the pockets of ratepayers, and let me assure him I share his concern. I also share his concern for the small producers of natural gas, who may indeed require some assistance.

Nonetheless, both issues are irrelevant to this debate. It is for state public utility commissions to decide how much money goes to companies and how much to ratepayers. And with regard to assisting natural gas producers, I would point out that there are other ways to help Kansas producers than by taking it directly from the pockets of my constituents or those residing in Missouri, Illinois, Iowa, Ohio, California or any of the other states owed refunds.

I would also posit that my good friend from Kansas may be pursuing an avenue that may ultimately prove unconstitutional since his legislation appears to have the effect of altering a final judgement by the courts and, if enacted, could be considered a taking.

Frankly, I find it difficult to understand why we are having this hearing today. The final disposition of refunds of the Kansas ad valorem tax is an issue that is still pending before the courts. Why should Congress legislate at this time? The producers are spending lots of their hard earned money to appeal the 1997 court ruling and I think it would be wrong for this Committee to deny them their day in court. Furthermore, if the issue is small, hardship cases, then I fail to understand these attempts to circumvent the FERC hardship process, because so far the Commission has granted exemptions in 6 out of the 11 cases it has reviewed to date. It certainly makes me wonder whether this process is truly driven by small producers, rather than large producers who already know they have the ability to pay the refunds with interest.

It's also unclear to me what action, if any, this Committee intends to take on the Kansas ad valorem issue. I note that this is being billed as an oversight hearing, yet the invitation letter to at least one of our witnesses asks them to comment on Mr. Moran's bill.

What is also unclear to me is the position and the procedures of the Federal Energy Regulatory Commission. I have a memorandum from FERC, with Mr. Smith's name on it, that went to our friends on the Appropriations Committee stating that Chairman Hoecker would not oppose the language that was included in the Supplemental Appropriations bill. Now the Roberts language amended the Natural Gas Policy Act which is within our jurisdiction, yet no one from FERC saw fit to consult with Chairman Bliley or me about our views on legislation affecting a law within this Committee's jurisdiction. I am curious how this position was arrived at and how FERC came to the decision to involve itself in this matter. Was an open public meeting held to consider this issue? Did the Commission vote on this matter, or was this memorandum only the position of one commissioner? If it was only Chairman Hoecker's position, what were the positions of the other Commissioners and are they aware that he intervened in this matter both here and at the White House? I would also like to understand why FERC took a position on an issue that is still pending in the courts and why Mr. Smith's testimony states that FERC has no position, when it's clear that the Chairman has taken a position in favor of one side's view in this matter. These questions must be answered because they raise serious concerns for me at a time when we are being asked to grant them *more* power in the area of electricity transmission.

Mr. Chairman, while I am certainly interested in hearing from our witnesses, it seems clear to me that this is a topic that, at the very least, is not yet ripe for legislative action. What may be ripe, however, is an oversight hearing on FERC and its procedures and I hope the Chairman will consider holding such a hearing before we take any action that would have the effect of increasing FERC's power.

Mr. BARTON. Does the gentleman wish to give an opening statement?

Mr. HALL. I have given my statement, Mr. Chairman. It was very unusual, I beat you here. First time in about five meetings.

Mr. BARTON. Not the first time and, hopefully, it won't be the last.

Well, the Chair would recognize himself for an opening statement.

We want to thank everyone for being here today, especially Congressman Moran. We understand that he has worked on this issue quite a bit.

Today's hearing is on the Kansas ad valorem tax refund issue. It is an important issue, and it is also an issue that is complex and has gone back and forth at the Federal Energy Regulatory Commission. It is an issue that I am personally deeply concerned about, and I have sent several letters to the various committees and to the Senate on this issue.

This is an issue that comes from the days when natural gas prices were regulated at the wellhead. It is an unfortunate issue that arises at a time when independent oil and gas producers in many parts of the country, including Kansas, are struggling for survival.

I am not going to recite the long history of the issue. I am sure the witnesses that we have before us today will do that much better than I could. I am going to say, though, that I am concerned that there are many small producers and royalty owners located in Kansas and also around the country today that they are facing a huge tax and penalty liability as a result of years of legal wrangling and of which in some cases they are just now becoming aware.

I believe that this is an issue of equity. I believe it is an issue of fairness.

Should producers and royalty owners be required to pay 13 years' worth of interest on a tax that they didn't know that they owed at the time that it was incurred?

Should they have known that it might be owed at some point in the future?

Should pipelines and local distribution companies be required to prove their claims for refunds before producers are ordered to pay those claims?

Are natural gas consumers harmed if the interest payments on the tax refund are waived?

I hope today's witnesses can shed light on all of these questions and other questions that other members of the subcommittee may have as the hearing progresses. If this hearing reveals that congressional action on the issue is warranted, I would be very interested to learn if the interests believe that Congressman Moran's bill that is pending before the Congress is the right approach to resolve the issue at this point in time.

Again, I want to welcome everyone to today's hearing. I am sure that it will be very informative.

Are there other members present that have not been given a chance to give an opening statement?

Mr. Shimkus, do you wish to give an opening statement?

Mr. SHIMKUS. I have already given it.

Mr. BARTON. Seeing no other members present, all members shall have the requisite number of days to put their statement in the record at the appropriate point in time.

[Additional statements submitted for the record follow:]

PREPARED STATEMENT OF HON. TOM BLILEY, CHAIRMAN, COMMITTEE ON COMMERCE

Mr. Chairman, thank you for holding this hearing on the Kansas *ad valorem* tax refund issue. I know natural gas producers and royalty owners are anxious to see this issue resolved quickly. However, I believe on complicated issues such as this one, holding a hearing and developing a record for action is important.

Importantly, this issue arises from the days of natural gas price controls and serves as a reminder as we work on electric utility restructuring that free markets are preferable to government intervention. It is unfortunate that many years after wellhead prices of natural gas have been decontrolled, natural gas pipelines, producers and customers are still embroiled in battles over these regulations. I hope today's hearing can help us better understand this issue and discover ways to avoid such controversies in the future.

I look forward to hearing the testimony of the witnesses. Thank you.

PREPARED STATEMENT OF HON. KAREN MCCARTHY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MISSOURI

Thank you Mr. Chairman. I would like to thank the Chairman for holding this hearing on this issue which is so vitally important to Missouri and I would like to commend the Chairman for extending an invitation to my good friend and former colleague, Ms. Sheila Lumpe, Chair of the Missouri Public Service Commission. I would also like to recognize my friend and neighbor, Ms. Carla Stovall, Attorney General for the State of Kansas.

We are here today to discuss the Kansas *ad valorem* tax and the legislation that has been introduced on this bill by our colleague Rep. Jerry Moran, H.R. 1117. Our task here today is to ensure that equitable and just results are reached for all parties involved.

For over 15 years, the issue of whether and how much of a refund to be paid natural gas consumers has been litigated before the D.C. Circuit and before FERC. After years of litigation, the D.C. Circuit Court of Appeals finally determined that natural gas producers in the State of Kansas owed refunds on the amounts charged in excess of the maximum lawful price dating back to 1983, when the challenge to the Kansas *ad valorem* tax was first made and sellers were first put on notice of the potential refund obligation.

In response to these determinations, legislation was introduced to mandate that only the amount charged, and not the interest on these amounts be paid by the producers. H.R. 1117 and advocates of this legislation argue that the measure presents an equitable solution to the decision reached by FERC and the D.C. Court of Appeals, which they say will unreasonably burden small businesses and hurt the economy.

Arguably, the final determination which has been reached as a result of this litigation is equitable and just. Interest on the amounts paid is the only way to ensure that those so charged receive the full time value of their money. Since 1989, the Missouri Public Service Commission has been actively seeking recovery of the Kansas *ad valorem* refunds which are due to consumers in over 20 states, including Missouri. It is estimated that Missouri consumers are owed upwards of \$60 million. Even with the notice as early as 1983 that they might be responsible for refunding monies, consumers in states, such as Missouri, have been paying rates above the maximum lawful amount.

It would be unwise for this body to reverse the lengthy due process delivered within the judicial and administrative branches of our government and essentially legislate the taking of property, that is the taking of the refund and interest owed consumers in this country, including those in the State of Missouri.

I look forward to hearing the testimony today on H.R. 1117 and the Kansas *ad valorem* tax, and yield back the balance of my time.

Mr. BARTON. The Chair would call the first witness to today's hearing, the Honorable Jerry Moran from the great State of Kansas.



Mr. Moran, welcome to the committee. Senator Roberts sends his greetings. He called me earlier this morning to say that he couldn't be here, but he knew that you would do an outstanding job on the issue and that we would fairly inform the committee of the pros and cons of the issue. We will put your entire statement in the record, and we would recognize you for such time as you may consume. Hopefully, that will be less than 7 or 8 minutes.

**STATEMENT OF HON. JERRY MORAN, A REPRESENTATIVE IN  
CONGRESS FROM THE STATE OF KANSAS**

Mr. MORAN. Mr. Chairman, thank you for your admonition on time.

I appreciate Mr. Robert's kind remarks. I wish he would say them more often in Kansas as well.

It is a delight to be here on this issue. I wish the issue didn't exist, and I was somewhat disconcerted to hear Mr. Hall say all solutions are not very good, but I come with the suggestion of at least one.

Imagine receiving a notice from the IRS saying that, while you had paid your taxes in full 15 years ago, the IRS has changed its mind on how you figured your taxes and could you please pay an additional \$5,000 and, oh, by the way, \$10,000 in penalty and interest. We would not tolerate this type of retroactive taxpayer abuse by the Internal Revenue Service. However, this is essentially what another government agency has done to Kansas natural gas producers and royalty owners.

I do appreciate the opportunity to be here and discuss an injustice that is being perpetrated on many of my constituents. At issue is whether Kansas natural gas producers could pass through to their customers the Kansas ad valorem tax. In the regulated energy marketplace in the 1980's these decisions and the resulting price charged for natural gas were made by the Federal Power Commission, the predecessor to the Federal Energy Regulatory Commission.

FPC and later FERC consistently ruled that Kansas ad valorem taxes could be included in the price of gas paid to these companies, to the producers, by their pipeline customers. It was not until 1993 that FERC reversed its previous rulings. FERC's reversal and subsequent court case provided the charges for ad valorem taxes should not have been passed through from 1983 to 1988 and must now be refunded. In addition, interest penalties were assessed that now more than double the amount of tax in question.

Let me make several points as we review this issue.

First, my constituents and all royalty owners and producers followed all applicable laws, rules and regulations. The Federal agency responsible for regulating these matters explicitly gave its blessing to the pass through of these taxes. Many gas contracts were written with specific reference to FERC's ruling on the matter. It was not a gray area, it was not subject to interpretation, and none of these individuals could, should or would have been expected to have handled it any differently.

There are those who would claim that producers and royalty owners somehow should have known that FERC would change its ruling. This is simply not the case. FERC ruled on this issue three

separate times in 1983, 1986 and 1987. Each time, FERC ruled that the taxes were correctly applied.

I don't know how many times we need to hear from a Federal agency to believe it, but I suspect that after three rulings since the issue was questioned and two rulings prior to 1983 that producers rightfully believed they were following the law. After five separate successful rulings on my own tax return from 15 years ago, I might even be willing to throw the tax return away and sleep well at night.

Second, a 15 year reach-back is outrageous. We have all heard of cases of unfair, arbitrary, irrational, convoluted decisions by Federal Government agencies, but this one takes the cake. To reverse a decision and then even go back over 15 years and force the payment of refunds with interest isn't only unfair, it is unconscionable. Why is there no statute of limitations? What about *ex post facto*? This country was born out of protest against this type of improper governmental conduct, and we should not stand for it in this case.

Third, the decision is devastating to producers and offers little for consumers. For royalty owners and small businesses this decision could not have come at a worse time. We read of the consolidation of the major oil and gas companies due to difficult times, but we do not as easily see the hundreds of small businesses that have closed their doors, laid off employees, gone bankrupt. In Kansas alone, the oil and gas industry has laid off 5,000 employees in the last year.

The burden on small businesses as a result of this situation is enormous. For example, Mid Continent Energy, a small Kansas company with two employees, owes \$244,000. Several of my elderly constituents have written and described bills they have received well over the value of their annual payments they receive from Social Security.

A typical example is Mrs. Betty Shingler of Wichita, Kansas. She along with her husband were the owners of a company called Aurora, Inc. Early in the 1980's, Mr. and Mrs. Shingler, with outside investors, owned six gas wells. Today, Mrs. Shingler, who lost her husband 3 years ago, now faces a \$19,000 bill.

FERC's decision not only affects the companies that explore for and produce natural gas, their far-reaching decision has a terrible impact on royalty owners. Royalty owners are those who own the land under which the natural gas is located, often the farmers and ranchers of southwest Kansas.

Today you will hear examples from property owners who have been unknowingly attacked by this situation. You will also hear about consumers and how they are owed this refund. This issue deserves your review.

Of the eight pipeline companies involved in obtaining the refund and interest, two have already filed with FERC to keep the refund and not pass it on to consumers. My counterparts in the Senate, Senator Roberts and Senator Brownback, have called for a GAO investigation on the distribution of refunds; and I fully support that request. One would like to think that each dollar collected would be returned to the original customer. However, after 15 years, many people have moved, retired or passed away. What happens

to the money when customers can't be located? Could this be why pipelines fight this issue so aggressively?

Although the damage is huge, the benefits are small. For the average household consumer, this refund is minimal and will likely be prorated. For example, in Kansas a typical house receiving gas from the Greeley Gas Company using 100 mcf per year will receive an estimated \$6 refund. Among the estimates I have seen, a typical household across the country would receive around \$15 or just about a little over a dollar a month for 12 months.

Keep in mind that Kansans, as well as producing the gas, are also the largest recipients of the refunds. Representing the largest positions on both side of this issue, I introduced what I consider compromise legislation that has been referred to this subcommittee, H.R. 1117. This legislation attempts to strike at the basic requirement of fairness. Under the bill, the amount of disputed tax would be collected, but an interest penalty would not be assessed and the refunds required would be required only to the extent that they will be received by the ultimate consumer.

While I contend that the pass through of a tax, after being approved by FERC five times, should be allowed to stand and no refunds ordered, I introduced this bill as a compromise to try and protect the hundreds of individuals who had always acted in accordance with the law.

Again, I thank this committee for their time and attention. I would be a happy to answer any questions.

And I also welcome my Kansas colleagues, including the Attorney General of the State of Kansas, Carla Stovall.

Mr. BARTON. Does that conclude your statement?

Mr. MORAN. It does, Mr. Chairman.

[The prepared statement of Hon. Jerry Moran follows:]

PREPARED STATEMENT OF HON. JERRY MORAN, A REPRESENTATIVE IN CONGRESS  
FROM THE STATE OF KANSAS

Imagine receiving a notice from the IRS saying that, while you had paid your taxes in full fifteen years ago, the IRS has changed its mind about how you figured your taxes and could you please pay an additional \$5000 and another \$10,000 in penalty and interest. We would not tolerate this type of retroactive taxpayer abuse by the IRS. However, this is essentially what another government agency has done to Kansas natural gas producers and royalty owners.

I appreciate having the opportunity to be here to discuss an injustice that is being perpetrated on many of my constituents. At issue here is whether Kansas natural gas producers could pass through to their customers the Kansas ad valorem tax. In the regulated energy marketplace in the 1980's these decisions and the resulting prices charged for natural gas, were made by the Federal Power Commission (FPC), the predecessor to the Federal Energy Regulatory Commission (FERC).

In several rulings on this issue, FPC and later FERC, consistently ruled that the Kansas ad valorem tax could be included in the price of gas paid to these companies by their pipeline customers. It wasn't until 1993 that FERC reversed its previous rulings. FERC's reversal and subsequent court case provide that charges for ad valorem taxes should not have been passed through from 1983 to 1988 and must now be refunded. In addition, interest penalties were assessed and now more that double the actual amount of tax in question.

I would like to make several points as we review the issue today:

*First, my constituents, and all royalty owners and producers, followed all applicable laws, rules and regulations.* The federal agency responsible for regulating these matters explicitly gave its blessing to the passthrough of taxes. Many gas contracts were written with specific reference to FERC's rulings on the matter. This was not a gray area, was not subject to interpretation and none of these individuals could, should or would have been expected to have handled it any differently.

There are those who would claim that producers and royalty owners somehow should have known that FERC would change its ruling. That is simply not the case. FERC ruled on the issue three separate times in 1983, 1986, and 1987. Each time, FERC ruled that the taxes were correctly applied. I don't know how many times we need to hear from a Federal agency to believe it, but I suspect that after three rulings since the issue was questioned and the two rulings prior to 1983 that producers rightly believed they were following the law. After five separate successful rulings on my taxes from 15 years ago, I might even throw away my returns and sleep well at night.

*Second, a fifteen year reach-back is outrageous.* We have all heard of cases of unfair, arbitrary, abusive, irrational or convoluted actions by federal government agencies, but this one takes the cake. To reverse a decision and then go back over 15 years and force the payment of refunds, with interest, isn't just unfair, it's unconscionable. Why is there no statute of limitations? What about ex post facto? This country was born out of protest against this type of improper governmental conduct. We should not stand for it in this case.

*Third, the tax is devastating for producers and offers little for customers.* For royalty owners and small businesses this tax could not have come at a more difficult time. We read of the consolidation of the major oil and gas companies due to the difficult times, but we do not so easily see the hundreds of small businesses that have gone bankrupt, gone through layoffs, or otherwise been forced to close their doors. In Kansas alone, the oil and gas industry lost some 5,000 jobs in the last year.

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Keep in mind, that Kansans, as well as producing the gas, are also the largest recipients of the refunds. Representing the largest positions on both sides in this issue, I introduced the compromise legislation that has been referred to this subcommittee, H.R. 1117.

This legislation attempts to strike at the basic requirement of fairness. Under the bill, the amount of disputed tax would be collected, but an interest penalty would not be assessed and the refunds required only to the extent they will be received by the ultimate consumer.

While I contend that the pass through of the tax, after being approved by FERC five times, should be allowed to stand and no refund ordered, I introduced this bill as a compromise to try and protect the hundreds of individuals who had always acted in accordance with the law.

Again, I thank the committee for their time and attention and would be happy to answer any questions.

Attached is just one example for the committee's review. In this situation, the accused company was not even involved in the gas business during the time in question.

ARGENT ENERGY, INC.  
May 11, 1999

Congressman JERRY MORAN  
1519 Longworth  
Washington, D.C. 20515

Re: Refunds of Kansas *ad valorem* tax reimbursements (Federal Energy Regulatory Commission Docket Nos. RP97-369-000, et al.)

DEAR CONGRESSMAN MORAN, Argent Energy, Inc. is a small independent Kansas oil and gas producer/operator. I formed Argent Energy November 1, 1989, three years after the 1986 oil price collapse. At its inception, the company had no producing properties, only some cash the stockholders had contributed to get it started. Argent has survived and grown both by successful exploratory drilling and by acquiring producing properties. Additionally, it operates producing properties owned by others, and receives compensation for these services. It has three employees.

Early in 1993, Argent purchased working interests in 27 wells from Kiwanda Energy, Inc. for \$195,000. Ten of these wells were oil wells, two were saltwater disposal wells, and fifteen were gas wells. Prior to purchase, Argent had no connection whatsoever with any of those wells. The sales were an arms length, contractual transaction wherein Kiwanda agreed to indemnify and hold Argent harmless from all claim, liabilities, penalties, and losses arising out of any obligations incurred by Kiwanda concerning these properties (except as specifically assumed by Argent). Further, Kiwanda warranted that these properties were unencumbered and were free and clear of adverse claims.

A few weeks after the purchase of these properties, Argent terminated the gas sales contract Kiwanda had in place with Northern Natural (now Enron). Under that termination agreement Northern discharged Argent (and its officer, directors, agents, and employees) from "any and all liabilities, claims and causes of action, whether known and asserted or hereafter discovered, arising out of or relating to said contracts..." Argent then entered into its own sales contract with Northern.

By letters dated October 5, 1998, and October 12, 1999, FERC directed Kiwanda and its predecessor, Exploration and Production, Inc. to make payments for stated amounts due for reimbursement of Kansas *ad valorem* taxes paid them during the period 1983 to 1988. Since both Kiwanda and its predecessor were now out of business, the letters were sent to those two entities at Argent's mailing address. By letter dated November 2, 1998, Argent informed the Commission that it was not affiliated with and was not a mail drop for either Kiwanda or its predecessor. Further, Argent did not at that time own an interest in these properties, and indeed was not even in existence during the time of the alleged reimbursements, thus could not have received any such reimbursements.

In spite of this reply, Argent received a letter from the FERC dated March 26, 1999, in which the Commission appears to have determined that Argent is indeed liable for these reimbursements as a successor to Kiwanda and its predecessor. The total of these alleged reimbursements plus interest is \$855,147.60. I'm not sure but that we would have been better off had we thrown the first letters in the trash unopened. Argent has been forced to retain legal counsel to defend itself from being held responsible for an amount more than six times what it paid for these properties in 1993.

I still don't understand how a 1974 FPC ruling which allowed pass-through of Kansas *ad valorem* taxes (which was consistently upheld), could be *reversed retroactively for fourteen years, have fourteen years of interest applied*, then be assessed on natural gas producers who had complied with the law in effect at the time of these reimbursements. I just cannot comprehend such an action occurring in this country—and I cannot believe that a regulatory body constituted in this country could hold Argent Energy, Inc. liable for repayment of reimbursements which it did not receive, on properties it did not own, during a time period before it existed, and having no possibility of recoupment from the now non-existent seller.

Congressman Moran, I join many Kansas gas producers in expressing my appreciation to you for your understanding and help. Your authoring of proposed legislation to remove the interest imposed on the repayment demanded on these reimbursements is indeed meaningful, both to Kansas royalty owners and to the producers. In the case of Argent Energy, however, *the entire liability is inequitable*. We have filed, through our attorneys, a reply to the FERC letter of March 26, 1999. I would hope that you will be able to monitor Argent's efforts to remove this liability. The filing is under Docket No. SA99-5-000. If there are further steps I should

be taking, please let me know, and if I can furnish you with further documentation, I'll be happy to. Thank you for your consideration.

Sincerely,

JAMES C. REMSBERG  
*President*

Mr. BARTON. The Chair would recognize himself for the first 5 minutes of questions.

Is there any estimate on the number of original consumers that are still in the area that can be found in order to give the direct refunds to?

Mr. MORAN. I have not seen any kind of specific numbers. I think there is a general agreement that there is a very difficult circumstance that—locating potential consumers out there; and the ones that were ultimately entitled perhaps to the refund, as I said in my testimony, may not be living and addresses cannot be found.

Mr. BARTON. Well, assuming that you can locate some of the original payers of the tax, consumers that consumed the gas, but let's just for estimation purposes say that only about 50 percent of the original consumers can be located and identified, so that there is 50 percent of the remainder that cannot be and that 50 percent of the funds and 50 percent of the interest and 50 percent of the penalty is just sitting out there in a pot, is there a consensus on what is done with that money?

Mr. MORAN. I would guess there is great disagreement as to what should be done with that money. That is an issue between the royalty owners, the natural gas producers, the working interest, and the pipelines; and that is an issue that I think is awfully important.

Mr. BARTON. There is no defined protocol. There is not an automatic lump sum payment to the State of Kansas or lump sum payment to some charity in Kansas City or—

Mr. MORAN. Mr. Chairman, there is not.

Mr. BARTON. [continuing] or congressional campaign committee account.

Mr. MORAN. Certainly that is one I would be aware of, and I am not.

Mr. BARTON. Okay. In Kansas and in the general public, is this an issue that is talked about? Is this a front page story or is this pretty much an inside Washington and royalty owner producer pipeline story?

Mr. MORAN. No, I wish it was much more of a story than it has been. It is a significant issue in Kansas. It has been an issue of the Kansas legislature. Our Governor, Governor Graves, has come to Washington to meet with FERC, has written the President. This has a major impact upon Kansas.

The Governor, one of his concerns is the resulting demise of the oil and gas industry as a result of the refunds, the penalty and interest at a time when there is no way that they can absorb those costs, results in less exploration, less drilling, and businesses going out of business.

The State of Kansas is concerned about their financial security as far as a State. The revenue estimates in Kansas are impacted as a result of this issue being forced upon our working interest and royalty owners.

Mr. BARTON. What is the status right now? I know Senator Roberts had an amendment in one of the supplemental appropriation bills that came over from the Senate. What is the current status of this in terms of a resolution of the issue in the Congress?

Mr. MORAN. I know of nothing close to a resolution of this issue in Congress.

There was an effort made to prohibit the collection of the penalty interest in the appropriation process in the emergency supplemental which was not included in the conference report. And to my knowledge, you, Mr. Chairman, and Mr. Hall, your subcommittee is the first to take a serious look at a serious issue.

Mr. BARTON. So have you gotten any input or feedback from either the Republican or Democrat leadership in the House on your bill that they support it, oppose it, neutral, haven't had a chance to look at it?

Mr. MORAN. I certainly would not admit nor would it be true that I haven't had the chance to talk about it. I have talked to the leadership, members of this committee, members of the full committee as well as Republican leadership of the House stressing the importance of this issue to many producers and to many royalty owners.

I think it is a very difficult issue for anyone to understand. If you are not knowledgeable in what a royalty interest is and what FERC does in the regulated nature of the gas industry in the 1980's or many struggle to know what an ad valorem tax is. It is a very difficult issue for me as a Member of Congress to describe to my colleagues and get sympathy.

I think the broad picture of how can any Federal agency do this to any taxpayers, to any business, through changing its mind 15 years after the fact, I think that is a bigger issue and easier one for me to talk about.

Mr. BARTON. My time is about to expire. But if I were to say this is an example of a tax that was assessed, when it was incurred it was passed through, it was paid, legally, and then a Federal agency changed its mind after the fact, how far off would I be from the truth?

Mr. MORAN. I think you accurately describe the truth.

Mr. BARTON. So that is not that complex an issue.

Mr. MORAN. If I could talk about it in a broad sense of how this could happen in any business, any Member of Congress, it is an easier issue to talk about.

Mr. BARTON. Okay. My time has expired.

The Chair recognizes the gentleman from Texas, Mr. Hall, for 5 minutes.

Mr. HALL. I didn't mean to be discouraging to you in my opening statement. But I sat where you sat back in the early 1980's when Hawkins Field and Exxon had their collision and I saw the situation there where a lot of little royalty owners were absolutely wiped out. And I don't know if that is going to be the situation in Kansas or not, but it appears if they follow the cases that were tried in the Hawkins Field case then you are going to have a lot of bankruptcy lawyers get rich in Kansas. Because they absolutely came back on them years later when they couldn't tell them anything they had done wrong and they couldn't tell them how they

could have corrected it if they had known what they had done wrong.

And yet Exxon has shareholders. They were subject to shareholder suits and litigated. They didn't litigate it in the Hawkins Texas County courts, you know. They went to the Federal courts. And Federal courts, somehow some—impressed by the way the local people felt, and the royalty owners wound up, many of them, with bills of \$100,000, \$150,000 years and years and years later to pay, not understanding why they had to pay and where they were going to get it.

And there was—over a period of about 2 or 3 years there I think that the companies did their best to settle as many of them as they could. But it was a disaster and still, in my district, suffering; and, of course, there is nothing good has happened to the oil and gas people in the last 10 years.

It is a terrible time for you to be sitting where you are, doing what you are doing. And I admire you for doing it, but I must warn you that if you haven't read that series of cases—and I am sure you have and followed the Hawkins Field—I suggest you do so. Because we were sitting there, we didn't hate Exxon for what they did, because they probably had to do what they did to stave off their own shareholders.

I thought FERC was the enemy there and their delay and dilatory tactics. It just seemed that they were no help, really, to the royalty owners in the final analysis.

So what does your bill do? I haven't had a chance to read it.

Mr. MORAN. Mr. Hall, I appreciate having you on this committee with your knowledge of what happened in Texas and your understanding of the oil and gas industry.

Mr. HALL. Well, my knowledge and experience is bad, though, from where you sit.

Mr. MORAN. Appreciate your sympathy. And the Hugoton field, from which this gas is produced, is a Kansas, Oklahoma and Texas field. The reason this is a Kansas issue is because of the way they were treating Kansas ad valorem.

This bill does two things, Mr. Hall. It eliminates the interest that goes back to 1983, leaving the principal amount of the refund in place; and it also says that no amount should be collected that can't ultimately be received by the original consumer.

Mr. HALL. And would you say that knocks out the interest provision?

Mr. MORAN. That knocks out the interest provision.

Mr. HALL. Does your bill toll the interest or how does your bill handle it?

Mr. MORAN. The bill, Mr. Hall, is very straightforward. Basically says that no interest should be collected on this amount, the principal amount of the tax.

Mr. HALL. Think that will navigate the big court?

Mr. MORAN. One step at a time, Mr. Hall—

Mr. HALL. You have nothing to lose.

Mr. MORAN. [continuing] from my perspective.

Kansas has also attempted to address this issue in passing a statute of limitations to try to toll the collection for royalty owners.



Mr. HALL. Well, ours wound up in just absolute disaster for a lot of royalty owners; and a lot of people, like your folks, had no knowledge of what price was being charged and had no way to protect themselves even if they did and still—yet they didn't prevail at the courthouse. It was a pretty sad situation.

I yield back my time. I may think of something that will help you before we leave. But I will listen to the rest of the testimony.

Mr. MORAN. Thank you, Mr. Hall.

Mr. BARTON. I see Mr. Largent is not here.

The gentleman from Mr. Tennessee, Mr. Bryant, is recognized for 5 minutes.

Mr. BRYANT. Thank you, Mr. Chairman.

I agree with my colleague from Kansas that it is a very interesting issue and certainly one that you have a personal stake in in terms of your constituency. Do I understand that your bill would weigh the interest as well as the penalty in any such payments?

Mr. MORAN. That is correct. And, generally, the penalty and interest have been words that have been interchangeable as the parties have talked about this issue. It is basically interest that dates back to 1983. There is no additional penalty.

Mr. BRYANT. And interest would be calculated as straight percentage times whatever is owed per year?

Mr. MORAN. I am unable to determine exactly what interest rate is being charged, and I have been told anyplace from 6.5 to 12.5 percent. That would be an opportunity to find out some facts today perhaps from the testimony from FERC.

Mr. BRYANT. Now, in reading some of the other comments in advance, I understand that the other side of this position says that, well, these folks were on notice, it was being challenged, and therefore they should have taken that into consideration. And you said today that you had a number of successful rulings and, therefore, they should have felt comfortable knowing that they were acting correctly.

I share your concern, particularly with the smaller companies. To some extent, I guess, I really don't know enough about this issue to come down finally on one side on the other. But I understand something like 15 percent of the money involved here would have to come from small businesses and small producers.

Mr. MORAN. That is correct, Mr. Bryant.

Mr. BRYANT. Eighty-five percent would be from larger sources. How are smaller companies, the producers and the royalty owners, finding out about this liability?

Mr. MORAN. Well, that is a real problem, particularly for royalty owners. Many of them just received letters from the gas producers saying you owe X number of dollars and you have 10 days to pay that amount of money. The royalty owners are not parties to the litigation, are not in front of FERC. And we will have testimony today from the Southwest Kansas Royalty Owners Association in which you might—I know their testimony will describe this further.

But it is really like a shot in the dark. People who have no idea, had nothing to do with whether or not the tax was passed through by the gas company that is producing gas on their land, received a letter from the gas company saying we got to pay, you got to pay, we need money, and we need it quickly.

Mr. BRYANT. There is provision for some sort of waiver of this already for a hardship type situation. Does that require an application? How much of a cost from a legal standpoint would a small producer or a small royalty owner have to incur to successfully—or to apply for an application for hardship?

Mr. MORAN. FERC did provide for a hardship waiver, and there have been a number of applications for that waiver of which only a few have received favorable attention. And there are examples that will be given today of ones that most of us would think clearly a hardship exists. They have been opposed by other—the parties to the other side. I think every hardship waiver has been opposed.

And so it is a time-consuming, expensive process and one, again, that, particularly when it comes to royalty owners but also the small business natural gas companies, the producers, the working interest, they are not involved in the FERC proceedings and therefore don't know why they are the ones who have to come forward to present a case for a hardship in a very time-consuming and expensive way. This has been an ongoing, expensive legal battle for those that can afford lawyers.

Mr. BRYANT. I thank you, and I will yield back my time.

Mr. HALL. Mr. Chairman, can I correct one thing I said? I think I referred to FERC instead of the Department of Energy in the Hawkins case. You are dealing with FERC. FERC was the one that piddled around and didn't do anything about it for so long. But they are both north of the line, so it didn't make any difference.

Mr. MORAN. I am not sure where Kansas is, Mr. Hall.

Mr. BARTON. We will have to double check the meaning of "piddle" but it doesn't sound like it is positive.

Does the gentlelady from Missouri wish to ask questions of the first witness?

Ms. MCCARTHY. I will forego that as I have an opportunity twice each week as we commute back and forth together to pop those questions, and I will.

Mr. BARTON. The gentleman from Illinois, Mr. Shimkus, is recognized for 5 minutes.

Mr. SHIMKUS. Thank you, Mr. Chairman.

I am very interested in how our Federal agencies approach our citizens who should be clients. And we have all heard the IRS, and we have all heard the EPA, and now it looks like some of the concerns of how FERC is dealing with small business individuals.

But I do have a question, Jerry, on—in the committee memo it says, the FERC initially found that the tax was indeed a severance tax after appeal. This is in 1983. The FERC initially found that the tax was a severance tax. But, after appeal, the D.C. Circuit Court remanded the decision to the FERC which then determined that the tax was a property tax. And the D.C. Circuit Court's opinion was in 1988. Would that then have sent signal flags up that maybe there was a problem with the tax?

Mr. MORAN. The issue of whether or not the tax is a property tax or a severance tax is the key legal question before FERC in determining whether or not the tax can be passed through. If it is a production tax, it can be passed through according to FERC rulings and regulations in place at the time. If it was a property tax, it is

to be borne by the producer. So that has been the legal issue for which FERC ruled twice before 1988.

Then this issue was raised by the pipelines. FERC again ruled that it was a severance tax based upon production. The appeal went to the court that remanded it back.

And so two times before 1988 and three times subsequent this issue was determined by FERC. Ultimately, the reversal occurred in 1993. But even any kind of suggestion of notice we go back to 1983 in collecting the refund as well as the interest.

Mr. SHIMKUS. Right. Okay.

I yield back. That is the only question I had, Mr. Chairman.

Mr. BARTON. Thank you.

We have a pending journal vote. I would like to finish with Congressman Moran, if possible, before we recess to go vote.

We have Mr. Shadegg, Mrs. Wilson, and Mr. Rogan. In order of appearance, Mr. Shadegg would be recognized. If you could make your questions very brief so we can give Mrs. Wilson and Mr. Rogan a chance, too.

Mr. SHADEGG. I would happy to make my comments or my questions brief.

Congressman Moran, I wanted to give you an opportunity to respond to what I understand to be FERC's position regarding H.R. 1117 and let you have a chance to put on the record kind of your responses to the arguments that they make.

They argue, for example, that because the relief in H.R. 1117 is across the board relief, some who are not adversely affected could benefit from the relief granted in the legislation. I would like to give you a chance to respond to that.

Mr. MORAN. I am not certain who FERC would describe as those not adversely affected by this decision. There are those that have more financial ability to stand—withstand this assault. But all of them, large and small, wealthy and poor, have faced the circumstances of relying upon FERC decisions, a line of decisions over a long period of time. So I think that the argument that there are those that are not adversely affected, that premise makes it very difficult to respond to their suggestions.

Mr. SHADEGG. Second question I have, and it will be the last one, what about refunds that have already been made?

Mr. MORAN. There are—my understanding—and this is probably, Mr. Shadegg, a better question for other witnesses, but it is my understanding there has been some money paid into escrow, that some gas companies have paid. But this is still continuing to be a battle in front of the agency.

Mr. SHADEGG. Thank you. I yield back.

Mr. BARTON. Thank you. Thank you for being expeditious.

The gentlelady from New Mexico is recognized for, let's say, 2 minutes.

Mrs. WILSON. Mr. Chairman, I will yield my time. I have had at least one conversation with Mr. Moran, and I will clear up my questions I have privately.

Mr. BARTON. We thank the gentlelady.

And the gentleman from California is recognized for about 2 minutes.

Mr. ROGAN. Thank you.

I want to thank our colleague for joining us today. I am glad to have you here sharing this with us instead of just pestering me on the floor of the House as you have been doing on a regular basis.

Mr. Chairman, I have become intimately familiar with both the gentleman from Kansas' position and, more importantly, his constituents' position, because he has not allowed me a moment of peace since this issue erupted. I want to thank you for your leadership on this, Congressman Moran.

Mr. Chairman, I yield back.

Mr. BARTON. We have been piddling around, and now you have been pestering, and now we are trying to find peace. So maybe we can find some progress on this issue.

We are going to recess very briefly to go vote on the journal. I would encourage all our members to come back because we have six witnesses on the next panel, and both sides of the issue will be presented. We have a very balanced panel.

We want to thank you, Congressman Moran; and we will give you a chance to have the last word before we recess.

Mr. MORAN. Mr. Chairman, I would like to add for the record additional testimony and comments by constituents, including some letters I received.

I also appreciate your seriousness in addressing this issue. It is clear to me this is not just a hand-holding hearing, and I look forward to——

Mr. BARTON. We are serious about moving your bill or a version of your bill, based on what the next panel says; and Chairman Bliley is fully cognizant and very willing to address the issue seriously also.

We are going to recess until approximately 11 a.m. So I would encourage all members to come back very quickly.

[Brief recess.]

Mr. BARTON. The subcommittee will come to order.

Congressman Hall beat me into the room again, but he didn't beat me up to the podium.

We would like to welcome our second panel:

Mr. Doug Smith, who is the General Counsel for the Federal Energy Regulatory Commission.

Is Mr. Smith here in the room? Okay.

The Honorable Carla Stovall, the Attorney General for the great State of Kansas.

Is she in the room?

The Honorable Sheila Lumpe——

Ms. LUMPE. Lumpe.

Mr. BARTON. [continuing] from the Missouri Public Service Commission.

Is she in the room? Okay. If you will come forward please, ma'am.

Mr. Robert Krehbiel, the Executive Vice President for the Kansas Independent Oil and Gas Association.

Mr. John Majeroni, the Real Estate Department of Cornell University.

Is he here? Okay.

How close was I on your name?

Mr. MAJERONI. Just like macaroni with a J.

Mr. BARTON. Majereni, okay.

Mr. James Albright, the Associate General Counsel for New Century Energy Incorporated.

Okay. We want to welcome you.

We are going to yield to the gentlelady from Missouri to give special recognition to two of the witnesses.

Ms. MCCARTHY. Thank you, Mr. Chairman, and thank you for holding this important hearing.

I want to welcome a neighbor, Attorney General Stovall; and I am so glad that you are here.

I also want to welcome Sheila Lumpe who I served with, Mr. Chairman, in the Missouri legislature for more years than we care to admit. I thought she had a pretty tough job there. She was Chair of the Appropriations Committee, and I served on the Appropriations Committee for most of my 18 years there while chairing the Ways and Means Committee. I made her serve on that.

But I think she has the toughest job of all right now as the Public Service Commissioner, and she is doing an outstanding job. Mr. Chairman, she is leading the way on de-reg. She has formed task forces with the Commission and got in all the experts and is moving Missouri forward on that issue. And we look forward very much to your remarks today on the issue, very much on the ad valorem situation out there in Missouri, and I thank all the panelists for being there.

Thank you, Mr. Chairman.

Mr. BARTON. Mrs. Lumpe, if you need a negotiator to buy some rugs, Congressman McCarthy is the lady. I watched her in action in Morocco, and she bought a rug for about 10 cents on the dollar. I was very impressed that.

Ms. MCCARTHY. I learned that in Ways and Means.

Ms. LUMPE. Good experience on Ways and Means.

Mr. BARTON. We are going to recognize Mr. Smith, but the Chair wants to recognize a visitor in the audience who is a personal friend from Houston, Texas, who used to work at Atlantic Richfield Oil and Gas Company when I was a struggling young associate there. Mr. Earl Simms with Vastar is in the room, a good friend and gentleman and very bright person. So we are glad to have you.

Mr. Smith, we are going to recognize you for 5 minutes. We are going to go right down the line. Each of your statements is in the record in its entirety. And I am sure by the time we get to Mr. Albright the rest of the Congressmen will be back so we will have a spirited question and answer period. So Mr. Smith, you are recognized for 5 minutes.

Mr. HALL. Would the gentleman yield? Where did your friend go to school?

Mr. BARTON. I don't know where he went to school. He probably went to the University of Texas but I am just guessing.

Mr. SIMMS. I went to the University of Tulsa and got a graduate degree from the University of Texas in Dallas.

Mr. HALL. You just look like the kind of guy that was ruining the curve for guys like me.

Mr. BARTON. He was head of the policy shop at Arco Oil and Gas.

Mr. Smith is recognized for 5 minutes.

**STATEMENTS OF DOUGLAS W. SMITH, GENERAL COUNSEL, FEDERAL ENERGY REGULATORY COMMISSION; HON. CARLA J. STOVALL, ATTORNEY GENERAL, STATE OF KANSAS; HON. SHEILA LUMPE, COMMISSIONER, MISSOURI PUBLIC SERVICE COMMISSION; ROBERT E. KHREHBIEL, EXECUTIVE VICE PRESIDENT, KANSAS INDEPENDENT OIL AND GAS ASSOCIATION; JOHN MAJERENI, REAL ESTATE DEPARTMENT, CORNELL UNIVERSITY; AND JAMES D. ALBRIGHT, ASSOCIATE GENERAL COUNSEL, NEW CENTURY SERVICES, INC.**

Mr. SMITH. Mr. Chairman and members of the subcommittee, good morning. My name is Douglas Smith, and I am the general counsel at the Federal Energy Regulatory Commission. I am here today as a Commission staff witness and do not speak for the Commission as a whole or for individual members of the Commission. I appreciate the opportunity to appear before you today to discuss the complex issues surrounding the treatment of Kansas ad valorem tax payments for purposes of price regulation under the Natural Gas Policy Act.

The Natural Gas Policy Act, enacted in 1978, set ceiling prices for sales of natural gas by producers. Section 110 of the act allowed producers to charge their customers amounts in excess of the applicable ceiling prices to the extent necessary to recover State severance taxes attributable to the production of natural gas.

The application of section 110 to Kansas ad valorem taxes has a long litigation history which I will describe briefly. In 1983 a pipeline company purchasing gas from Kansas producers asked the Commission to find that the Kansas ad valorem tax was a property tax rather than a tax on the production of gas, and thus was not eligible for collection over and above the ceiling prices. In response, the Commission found that the Kansas tax could be recovered under section 110. In June 1988, the U.S. Court of Appeals for the D.C. Circuit found that the Commission had not adequately explained its decision to treat the Kansas tax as a tax on production and remanded the matter to the Commission for development of a cogent theory for distinguishing property and severance taxes for NGPA purposes.

In its order on remand, the Commission concluded that the Kansas ad valorem tax was a tax on property, not on production, and therefore producers could not recover it as an add-on under section 110. The Commission required Kansas producers to make refunds back to June 1988, the date of the court's Colorado Interstate decision. In 1996, the D.C. Circuit sustained the Commission's conclusion that the tax payments were not recoverable but held that refunds were due starting in 1983, not 1988 as had been ordered by the Commission.

In 1997, a number of producers asked the Commission to grant an across-the-board waiver of the obligation to pay interest on the required refunds for the period of 1983 through 1988. The Commission denied the request because such a waiver would be inconsistent with the court's decision requiring full refunds. The D.C. Circuit had already rejected the producers' argument that imposing refund obligations on them was unfair because they had relied on the Commission's prior rulings. The court had stated that any such reliance by producers would have been unreasonable.

A petition for review of the Commission's denial of a generic interest waiver is now pending before the D.C. Circuit and will be argued in September. Although the Commission denied the request for across-the-board relief from interest obligations, the Commission did provide for consideration of requests for special hardship waivers on a case-by-case basis.

Allow me now to describe briefly the current status of refunds related to the ad valorem tax. Refunds for 1988 through the end of price controls in 1993 amounting to \$125 million in principal and interest were paid by producers in 1994 and 1995. With respect to the earlier period beginning in 1983, producers owe refunds of approximately \$339 million, consisting of approximately \$129 million in principal and \$210 million in interest.

As of May 1999, producers had paid about \$95 million of these refunds for the 1983 to 1988 period. An additional \$100 million has been placed in escrow pending resolution of requests for refund adjustments now before the Commission.

The Commission's orders require with limited exceptions that interstate pipelines receiving refunds must flow those refunds through to their customers. The refunds will be flowed through to local distribution companies serving consumers in at least 13 States.

Let me now comment briefly on the bill introduced by Representative Moran. H.R. 1117 would make two changes to the NGPA. It would preclude assessment of interest or penalties in any refunds of pre-1989 State ad valorem taxes, and it would bar such refunds unless the refunds would be passed through to the ultimate consumers.

Neither the Commission as a whole nor Chairman Hoecker has taken a position on this legislative proposal. I do, however, have several observations concerning the proposed legislation.

First, the Commission recognized that the required refunds may cause some producers, and in particular some small producers, financial hardship. The Commission's September 1997 order stated that the Commission would consider waiver of an individual producer's obligation to refund both principal and interest in cases of special hardship. The Commission considers such petitions for waiver on a case-by-case basis. An across-the-board waiver of interest as proposed in H.R. 1117 would give all Kansas producers, without regard to hardship, relief from the interest component of the refund obligation. If interest is not provided in refund amounts, consumers would not receive full compensation for the earlier overcharges because the refunds would not reflect the time value of money. The Commission's regulations concerning refunds provide for appropriate interest to be paid in connection with all refunds.

Second, although H.R. 1117 would preclude penalties, penalties are not an issue in these cases. The Commission has not imposed any penalties on the producers. The assessment of interest in refund calculations is not intended to penalize the producer but rather to fully compensate the consumer for overcharges paid years earlier.

Third, H.R. 1117 would preclude refunds unless the purchaser demonstrates that the refunds will be passed on to ultimate consumers. The Commission's orders require interstate pipelines to

flow through all refunds to their consumers with an exception for three pipelines that have settlements with their customers permitting the pipelines to retain the refunds.

Mr. BARTON. The gentleman's time has expired about 2 minutes ago. Can you summarize your summary rather quickly, please.

Mr. SMITH. I will do so.

Finally, there are some questions about the intended effect of the legislation on refunds that have already been paid with respect to the period prior to 1989. As I mentioned, some refunds were made in 1994 and 1995 with respect to the 1988 tax year and \$95 million in refunds have been made with respect to the earlier time period. In order to minimize costly litigation in this protracted dispute, any legislation in the area should be as clear as possible as to the intended effect with respect to refunds already made.

The Commission is in the unenviable position of trying to bring to closure this dispute that lingers from an earlier era of pervasive Federal regulation of natural gas prices. The Commission will continue to apply the applicable law and consider the equities on all sides—producers, consumers, pipelines, and States—in working this matter through to completion in a timely manner.

Thank you for the opportunity to testify.

[The prepared statement of Douglas W. Smith follows:]

PREPARED STATEMENT OF DOUGLAS W. SMITH, GENERAL COUNSEL, FEDERAL ENERGY REGULATORY COMMISSION

Mr. Chairman and Members of the Subcommittee: Good morning. My name is Douglas Smith, and I am the General Counsel at the Federal Energy Regulatory Commission. I am here today as a Commission staff witness, and do not speak for the Commission itself or for individual members of the Commission. Thank you for the opportunity to appear before you today to discuss the issues surrounding the treatment, for purposes of price regulation under the Natural Gas Policy Act, of payments of *ad valorem* taxes to the State of Kansas by natural gas producers.

The central issues—Do Kansas producers owe refunds of amounts collected in excess of the statutory ceiling prices? For what time period are refunds due? Should refunds include interest on overcharges?—have been extensively litigated before the Commission and the courts beginning in 1983. H.R. 1117, which would preclude the inclusion of interest in any refunds ordered, would have the effect of modifying the outcome of Commission orders implementing a 1996 decision of the United States Court of Appeals for the District of Columbia Circuit requiring producers to refund all Kansas *ad valorem* tax reimbursements they received from their customers from October 1983 through the removal of federal price ceilings on January 1, 1993.

I will describe the background and history of the dispute concerning Kansas *ad valorem* taxes, discuss the current status of refunds and requests for waivers, and comment on issues raised by H.R. 1117.

*Statutory Framework*

Before 1978, the Commission regulated sales by natural gas producers under the Natural Gas Act (NGA), establishing just and reasonable rates to be charged by producers.

The Natural Gas Policy Act of 1978 (NGPA) replaced the Commission's NGA regulation of producer sales with a system of congressionally specified ceiling prices that producers could charge for their sales of natural gas. NGPA section 110 allowed producers to charge their customers amounts in excess of the applicable ceiling prices "to the extent necessary to recover... State severance taxes attributable to the production" of natural gas. Section 110 defined severance tax as "any severance, production, or similar tax, fee, or other levy imposed on the production of natural gas" by a state. The Wellhead Decontrol Act of 1989 ended NGPA regulation of all sales by natural gas producers effective January 1, 1993.

*History of the Case*

The State of Kansas has charged natural gas producers an *ad valorem* tax with respect to natural gas in Kansas since before the enactment of the NGPA. In 1974,



the Commission's predecessor, the Federal Power Commission (FPC), held that Kansas producers could recover the cost of the Kansas *ad valorem* tax as an add-on to the national just and reasonable rates the FPC was then establishing for sales of natural gas by producers. Opinion No. 699-D, 52 FPC 915 (1974). The FPC held that the Kansas *ad valorem* tax could be considered as similar to a severance tax because it was based largely upon production factors.

Following the enactment of the NGPA, the Commission similarly treated the Kansas *ad valorem* tax as a severance tax that producers could recover as an add-on to the ceiling prices under NGPA section 110. However, in 1983, Northern Natural Gas Company, a pipeline company purchasing gas from Kansas producers, asked the Commission to reverse that ruling. It argued that the Kansas *ad valorem* tax was a property tax on the value of the gas in the ground, rather than a severance tax on the production of gas, and thus producers should not be permitted to recover the Kansas *ad valorem* tax as an add-on to the ceiling prices. Northern Natural argued that the Commission had made a similar finding with respect to Texas' *ad valorem* tax. In 1986, the Commission upheld its earlier rulings that the Kansas *ad valorem* tax could be recovered as an add-on to the ceiling price, while the Texas *ad valorem* tax could not. *Sun Exploration & Prod. Co.*, 36 FERC ¶61,093 (1986), reh'g denied sub nom. Northern Natural Gas Co. 38 FERC ¶61,062 (1987).

In June 1988, the U.S. Court of Appeals for the D.C. Circuit critically reviewed the Commission's analysis of the Kansas tax, and found that the Commission had not adequately explained its decision to treat the Kansas tax as a tax on production and had not adequately distinguished the Kansas and Texas *ad valorem* taxes. *Colorado Interstate Gas Co. v. FERC*, 850 F.2d 769 (D.C. Cir. 1988) (*Colorado Interstate*). The court therefore remanded the matter to the Commission for a more "cogent theory" of what distinguishes a production or severance tax which a producer can recover as an add-on under section 110 from a non-recoverable property tax. *Id.* at 773.

In a 1993 order on remand, the Commission set out the standards for determining whether NGPA section 110 permitted producers to recover a particular tax as an add-on to NGPA ceiling prices. Among other things, the Commission held that a recoverable severance tax is a tax on the value of the volumes of gas removed from the ground. A non-recoverable property tax, by contrast, is a tax on the value of the gas remaining in the ground, as well as on the value of wells and other production assets on the lease. Applying those standards, the Commission concluded that the Kansas *ad valorem* tax, like the Texas *ad valorem* tax, was a "tax on property, not on production," and, therefore, producers could not recover it as an add-on to the ceiling price under NGPA section 110. *Colorado Interstate Gas Co.*, 65 FERC ¶61,292 at 62,371 (1993), *order on reh'g*, 67 FERC ¶61,209 (1994).

However, the Commission required Kansas producers to make refunds only back to the June 1988 date of the court's decision in *Colorado Interstate*. The Commission held that, until the court's decision, producers could reasonably have relied upon the Commission's previously settled rule that the Kansas *ad valorem* tax could be recovered as an add-on to the ceiling price.

Producers appealed the Commission's decision, arguing that the Commission should have reaffirmed its prior determination that the Kansas *ad valorem* tax could be recovered as an add-on to the ceiling price, and, in any event, should have ordered refunds only prospectively from the date of its decision in 1993. The Public Service Company of Colorado, supported by the Missouri Public Service Commission, also appealed the Commission's order, arguing that the Commission should have required refunds back to 1983, when the qualification of the Kansas *ad valorem* tax as an add-on to the ceiling prices was first challenged.

In 1996, the U.S. Court of Appeals for the D.C. Circuit affirmed the Commission's holding that the Kansas *ad valorem* tax was a property tax that could not be recovered as an add-on to NGPA ceiling prices. *Public Service Company of Colorado v. FERC*, 91 F.3d 1478 (D.C. Cir. 1996) (*Public Service*). However, the court rejected the Commission's finding that, before June 1988, producers had reasonably relied on the Commission's prior rule that the Kansas *ad valorem* tax could be recovered as an add-on to the ceiling price and thus that refunds should not be required before that date. The court explained its decision as follows:

[T]he status of the Kansas tax was expressly drawn into question in 1983 when Northern Natural first petitioned the Commission for a ruling that producers could not lawfully recover the tax under section 110. Once the recoverability of the tax was in dispute, we do not see how the Commission could possibly find that the producers reasonably relied upon continuing to recover it... Absent detrimental and reasonable reliance, anything short of full retroactivity (*i.e.*, to 1978) allows the producers to keep some unlawful overcharges without any justification at all. The court strongly resists the Commission's implication that the

Congress intended to grant the agency the discretion to allow so capricious a thing. Still, we do not require refunds of taxes recovered with respect to production before October 1983 because there is before us no controversy over those monies.

*Id.* at 1490. Accordingly, the court concluded that the producers' liability for refunds should extend back to October 1983, the date when parties were given notice that the recoverability of the tax was at issue. The court remanded the matter to the Commission to implement the refunds. The Supreme Court declined to review the Court of Appeals' *Public Service* decision. *Public Service Company of Colorado v. FERC*, 520 U.S. 1224 (1997).

In late 1994, while the appeal of the Commission's 1993 order requiring refunds for the period 1988-1993 was pending, the producers paid the refunds for the 1988-1993 period. The producers paid approximately \$125 million, which included interest.

In May 1997, after the Supreme Court declined to review the *Public Service* decision, a number of producers asked the Commission, in considering the Court of Appeals' remand, to grant all producers an across-the-board waiver of any requirement that they pay interest on their refunds of the reimbursement of *ad valorem* taxes collected during the period 1983 through 1988. The threshold question for the Commission was whether a waiver of interest would violate the court's decision. The court held that "[p]roducers are liable to refund all Kansas *ad valorem* taxes collected with respect to production since October 1983." 91 F.3d at 1492. The Commission concluded that refunds without interest would not satisfy the court's requirement of full refunds. The Commission explained that both the Commission and the courts have consistently treated interest as a necessary element of full refunds because interest is necessary to reflect the time value of money. The Commission pointed out that its regulations require interest to be paid on refunds both to provide just compensation for the losses, or costs, imposed on those who have paid excessive rates and to reflect the benefits which were available to companies which collected excessive rates. *Public Service Company of Colorado*, 80 FERC ¶61,264 (1997), *reh'g denied*, 82 FERC ¶61,058 (1997).

The Commission found that the court's decision required rejection of the producers' equitable argument in favor of waiving interest. The producers argued that imposing interest charges on them was unfair because they had relied on the Commission's prior rulings that the Kansas *ad valorem* tax did qualify as an add-on to the ceiling prices. The Commission, however, stated that the court had already found any such reliance by producers was both "foolhardy" and unreasonable. 91 F.3d at 1490. The Commission thus concluded that the *Public Service* decision left it with little choice but to deny an across-the-board waiver of the requirement to pay interest on the refunds required by the court.

The Commission was mindful, however, that the refund obligation with interest could present serious financial problems to specific producers. Accordingly, the Commission stated that it would consider individual producers' requests for relief from the refund requirement based on their particular circumstances.

A petition for review of the Commission's decision is currently pending before the U.S. Court of Appeals for the D.C. Circuit, which has scheduled oral argument for September 7, 1999.

#### *Status of Refunds*

Based on the Commission's 1993 order, producers paid, in 1994 and 1995, \$125 million in refunds for the 1988-1993 period, which included interest. Because of the timing of the *ad valorem* tax bills, these refunds included the tax payments for all of 1988.

Since the Commission's September 1997 order implementing the court's decision, nine pipelines have reported to the Commission that producers owe refunds for the reimbursement of Kansas *ad valorem* taxes of approximately \$339 million for the 1983-1988 period. Of that amount, the Commission estimates that approximately \$129 million is principal. The remaining \$210 million is interest. Under the Commission's regulations, as set forth in 18 CFR § 154.501(d), interest is calculated from the date of collection from the customer based on the average prime rate for each calendar quarter as published by the Federal Reserve. As of May 1999, the producers have paid about \$95 million of refunds, which includes both principal and interest. Thus, producers still owe about \$244 million in refunds.

Approximately 130 requests have been filed with the Commission for waiver of all or part of a producer's refund obligation. The Commission has acted on eleven of those requests, granting six, denying three, and dismissing two as unnecessary. In general, the Commission grants such requests where the applicant can show that payment of the refund will cause it a special hardship. Where a producer's applica-

tion for relief contains insufficient information for the Commission to make a determination, the Commission's staff contacts the producer and indicates the type of information which it should file in order to support its application for a waiver.

The Commission's orders require that interstate pipelines receiving refunds must flow those refunds through to their customers, with the exception of three pipelines (Natural Gas Pipeline Company, ANR Pipeline Company, and El Paso Natural Gas Company) which have Commission-approved settlements with their customers that permit the pipelines to retain all refunds they receive in exchange for certain benefits they granted to their customers. The initial refund reports filed by the pipelines in May 1998 indicate that the amount those three pipelines may retain is \$4.9 million, or about 1.5% of the total \$339 million in *ad valorem* tax refunds. The remaining 98.5% of the refunds will be flowed through to at least 225 local distribution companies serving consumers in at least 13 states: Colorado, Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, Ohio, Texas, Wisconsin, and Wyoming.

#### *Proposed Legislation*

H.R. 1117 would add the following new section to the NGPA:  
Section 603. REFUNDS.

In the event any refunds of any rates and charges made, demanded, or received for reimbursement of State *ad valorem* taxes in connection with the sale of natural gas prior to 1989 are ordered to be made by the Commission, the refunds shall be ordered to be made without interest or penalty of any kind, and the refunds shall be required only to the extent that the purchaser demonstrates to the Federal Energy Regulatory Commission that the refund will be passed on to ultimate consumers of the natural gas.

Chairman Barton's letter of invitation asked for comments on this proposal to waive the inclusion of interest in refund amounts.

Neither the Commission as a whole nor Chairman Hoecker has taken a position on this legislative proposal. However, I do have several observations to make concerning the proposed legislation.

First, the required refunds may cause some producers, particularly some small producers, financial hardship. As described above, the Commission's September 1997 order stated that the Commission may waive an individual producer's obligation to refund both principal and interest in cases of special hardship. The Commission considers such petitions for waiver on a case-by-case basis. An across-the-board waiver of interest, as proposed in H.R. 1117, would give all Kansas producers, without regard to hardship, partial (*i.e.*, interest but not principal) relief without having to file with the Commission individual applications for relief from the refund requirement and supporting those requests.

If interest is not provided in refunds, consumers would not receive full reparation for the overcharges, because the refunds would not reflect the time value of money. This would be contrary to the Commission's regulations concerning refunds, which provide for appropriate interest to be paid in connection with all refunds. 18 CFR § 154.501 (1998). That requirement is consistent with a policy of requiring regulated entities that have overcharged consumers to provide full compensation for the overcharges.

Second, although H.R. 1117 would preclude penalties, penalties are not at issue in these cases. The Commission's orders described above provide that producers must pay interest on their refunds of Kansas *ad valorem* tax amounts, but the Commission has not imposed any penalties on the producers. The assessment of interest in refund calculations is not intended to penalize the producer, but rather to fully compensate the consumer for overcharges paid years earlier.

Third, H.R. 1117 would preclude refunds unless the purchaser demonstrates that refunds will be passed on to ultimate consumers. The Commission's orders require interstate pipelines to flow through all refunds to their customers, except for three pipelines that have settlements with their customers permitting the pipelines to retain the refunds. In those cases, in return for certain benefits the pipeline had granted to their customers, the customers had agreed to allow the pipeline to retain all refunds the pipeline received from the producers. *Natural*, 85 FERC ¶61,001 (1998); *El Paso*, 85 FERC ¶61,003 (1998); *ANR*, 85 FERC ¶61,005 (1998). The flow through of refunds by local distribution companies is a matter subject to state regulation.

Finally, the intended effect of the legislation on refunds already made is not clear. First, there is ambiguity with respect to refunds made after the Commission's 1993 order. By its terms, H.R. 1117 applies to the period before 1989. As discussed above, the 1993 Commission order provided that producers refund Kansas *ad valorem* taxes collected after June 1988. The 1993 order covered essentially all *ad valorem*

taxes producers collected with respect to their 1988 sales, because Kansas generally calculated its *ad valorem* tax bills due as of January first as late as November of the same year, and sometimes even later, and the producers then billed their customers for reimbursement for their 1988 *ad valorem* tax payments. The Commission required producers to refund all such amounts as overcharge occurring after the June 1988 cut-off date, and the producers refunded those amounts in 1994 and 1995. As now worded, the proposed legislation could be interpreted as invalidating the requirement in the 1993 order that the producers' 1988 refunds include interest, and producers might request the Commission to provide a means for them to recover that interest.

In addition, it is not clear whether the proposed legislation would apply to the interest component of the approximately \$95 million in refunds producers have already paid pursuant to the Commission's 1997 order. Thus, if the proposed legislation is enacted in its current form, producers might ask the Commission to provide a means for them to recover from pipelines interest already paid pursuant to the 1997 Commission order implementing the D.C. Circuit's *Public Service* decision. The pipelines could be expected to seek recovery of those amounts from their customers. In order to minimize further litigation of this protracted dispute, any legislation in this area should be clear as to its intended effect.

#### *Conclusion*

The Commission is in the unenviable position of trying to bring to closure this dispute which lingers from an earlier era of pervasive Federal regulation of natural gas prices. Even a decade ago, the court in *Colorado Interstate* noted the "special context" of this case—a dispute about the application of the arcane law of price regulation at a time when natural gas markets were moving to competitively determined prices—and observed that "FERC's task on remand may be about as inviting as having to make costly repairs on a building slated for demolition." 850 F.2d at 775. Nevertheless, the Commission will continue to apply the law and consider the equities on all sides—producers, consumers, pipelines, and states—in working this matter through to completion in a timely manner.

Thank you for the opportunity to testify this morning. I would be pleased to answer any questions you may have.

Mr. BARTON. Thank you. Attorney General Stovall, you are recognized for 5 minutes.

Ms. STOVALL. Thank you very much. I appreciate the opportunity—

Mr. BARTON. And put the microphone over there, please, ma'am.

#### **STATEMENT OF HON. CARLA J. STOVALL**

Ms. STOVALL. I appreciate the opportunity to be here and represent Kansas' concerns. We are very supportive of the legislation that Congressman Moran has introduced. We are grateful for the support of our entire congressional delegation. Congressmen Tiahrt, Ryun and Moore, also Senators Roberts and Brownback. It is an issue that has great implications for Kansas. And while general counsel Mr. Smith has said FERC is in the unenviable position of trying to resolve these issues, FERC's position is not as unenviable as those of the small producers in Kansas and our royalty owners. That is where the problem is.

Congressman Moran told you about the long history of the small producers in Kansas relying on decisions of FERC. In 1986 he mentioned that northern decision. Not only did FERC say it is okay for our producers to pass on that *ad valorem* tax, they did so with language that said it is clear beyond question that they can do that.

When the issue finally was reversed on behalf of FERC and they said we changed our mind now, it is not really a tax you can pass on, you need to rebate it. When the D.C. Circuit approved that decision, they actually said that producers in Kansas were foolhardy

to rely on FERC decisions and that our reliance was not reasonable.

I would suggest to you that what is not reasonable is changing those rules in the middle of the game and even changing what it is that Congress has said was appropriate. In 1978, when the Natural Gas Policy Act passed, in section 110 you specifically said an ad valorem tax like Kansas had can be passed on. So FERC not only has changed the rules on producers in Kansas and our legislature but they changed the rules on you as well. That is what we have a great problem with.

With regard to Congressman Moran's bill, it addresses two of the concerns. I wish that we could go back in some way, what the chairman suggested, and have a perfect resolution of the situation, which would be to suggest that no rebates be due at all, but Jerry's bill doesn't ask for that. It says merely two things. One is that claims of interest that now are argued to be due back to 1983 would be waived. We strongly believe that equity requires that. FERC had the case when the D.C. Circuit remanded the Colorado case back to FERC for further explanation, not to reverse it but to say explain to us again how it is that this qualifies. FERC had that case for 5 years without doing anything on it. For 5 years.

Once the D.C. Circuit said we are going to change the rules and you are going to owe this tax after all, those 5 years that FERC had the case and did nothing on it now counts against our Kansas producers. During those 5 years they wouldn't have had reason to think that the rules of the game were going to be changed in light of all those prior rulings. So the FERC delay has caused great problems.

Equity second requires, in my opinion, that the bill be passed because the producers were very responsible in relying on those decisions. I can't fathom how the D.C. Court would say they were foolhardy or unreasonable to rely on that administrative agency. I can't explain it.

Three, had the producers known this would be the ultimate result, they could 19 years ago have changed their practice. They could have not drilled wells, they could have capped wells, they could have altered production had they known this. But they didn't know this.

And fourthly, the Kansas legislature, had they known this, rules would change, could have taken action. They could have repealed the ad valorem tax. They could have increased the percent of severance tax perhaps to compensate knowing the severance tax is a pass-through. They could have changed the ad valorem tax to comply with the new regulations like Colorado and Wyoming to be sure that it passed through. But the legislature didn't know that they needed to do anything to protect Kansas consumers either.

What is important is that FERC has ordered the Kansas producers to pay 100 percent of the bills that the pipelines have sent to them by March of this year. They had to pay 100 percent of it. Although there has been no due process hearing to determine what amount of liability a producer might owe, the pipeline simply calculated what they believed it was, sent the bill to the producers, and they have been ordered to pay 100 percent of it. There is no

due process in that at all. That is one of the things that we find additionally unconscionable.

The producers have made those bills dependent on the fact they have assumed that the maximum lawful price was charged and on top of that was this ad valorem tax. Records that we have looked at shows that that is not true. FERC has ordered the rebate only when the maximum lawful price was exceeded by that tax. Sometimes the maximum lawful price was not charged. So the tax on top of that still fell below the maximum lawful price as authorized by statute. In that case no refund is owed. But without a due process hearing for our producers to determine those pipeline bills are accurate or inaccurate, the producers are absolutely in the untenable position of having to cough up tens of thousands of dollars, sometimes hundreds of thousands, without being able to have redress.

And because of the other provision of Congressman Moran's bill which says that if the money is not to be paid to the ultimate consumers, it is not collected, that tries to balance the interest of the consumers with those of the producers.

I thank the committee very much for the time to be here.

[The prepared statement of Hon. Carla J. Stovall follows:]

PREPARED STATEMENT OF CARLA J. STOVALL, KANSAS ATTORNEY GENERAL

#### INTRODUCTION

Chairman Barton, Vice-Chairman Stearns, members of the Committee. I am Carla J. Stovall, Attorney General for the State of Kansas. Thank you for the opportunity to appear before your subcommittee in support of House Bill 1117, which has been introduced by Representative Moran of Kansas and is supported by Congressmen Tiahart, Ryun, and Moore. Before detailing Kansas' support of this bill, I have been asked to give a brief overview of the laws and legal decisions which have brought us to the current situation.

#### HISTORIC REVIEW

In 1954, the United States Supreme Court held that the Natural Gas Act allowed the Federal Government, under the Interstate Commerce Clause, to control the price paid for natural gas at the wellhead if such gas was sold to an interstate pipeline. *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672 (1954). From that time to 1993, the Federal Government, through the Federal Power Commission (FPC) and later its successor agency, the Federal Energy Regulatory Commission (FERC), established substantially all of the rates that could be recovered by natural gas producers across the nation. In 1974, the FPC in Opinion No. 699 authorized pipelines to increase the ceiling rates under the Natural Gas Act by allowing producers to recover "production, severance, or other similar taxes." This was interpreted to mean that Kansas natural gas producers could charge pipelines the "Maximum Lawful Price" and, in addition, collect reimbursement for the Kansas *ad valorem* tax (Kansas did not have a severance tax until 1983).

In an effort to be absolutely certain of its interpretation, the Kansas Corporation Commission filed a request with FPC in August of 1974 seeking clarification of Opinion No. 699, concerning the right of producers to recover the Kansas *ad valorem* tax. The FPC responded on October 9, 1974 by issuing Opinion No. 699-D which reaffirmed that a proper interpretation of Opinion No. 699 allowed producers to increase the ceiling rates to recover their costs of the Kansas *ad valorem* tax imposed on natural gas production.

Four years later in the Natural Gas Policy Act of 1978, Congress codified (in Section 110) the FPC's earlier decisions, contained in Opinions No. 699 and 699-D, which allowed reimbursement of State "production" taxes. While Section 110 did not mention any specific state tax, the legislative history made it clear that the Kansas *ad valorem* tax was intended to be included as a tax allowed to be passed through. The Joint Explanatory Statement to the Conference Committee Report, accompanying the NGPA, noted that this cost included "any tax imposed upon mineral

or natural resource production *including an ad valorem tax or a gross receipts tax.*" (Emphasis added.)

In reliance upon FPC Opinions No. 699 and 699-D and Congress' passage of the Natural Gas Policy Act affirming those opinions, the Kansas Secretary of Revenue testified in 1981 before the Kansas Senate Tax Committee that was considering legislation which would have imposed a severance tax on natural gas production. In his testimony he accurately stated that the FPC had ruled that Kansas' current *ad valorem* property tax, as well as a severance tax if enacted, could be passed through to allow producers to recover the tax. In reliance on the FPC ruling and the Congressional action, the Kansas Legislature in 1983 passed a severance tax, justifiably believing that Kansas producers could recover the cost of both the severance tax and the *ad valorem* property tax. Consequently, during the period from 1983 until 1988, producers and royalty owners were collecting reimbursement of the Kansas tax from the pipelines under final, non-appealable FPC Orders.

In 1983, the year that the severance tax was passed by the Kansas Legislature Northern Natural Gas Co. (Northern) filed an application with the FERC to "reopen, reconsider and rescind" Opinion No. 699-D. Three years later, in 1986—a full twelve years after FERC issued Opinion No. 699-D authorizing "pass through" of the Kansas *ad valorem* tax—FERC rejected Northern's request stating that it was "**clear beyond question**, that the Kansas *ad valorem* tax is based, in large part, on gas production" (emphasis added), and re-affirmed its prior opinion which allowed the tax to be passed through. FERC denied Northern's request for rehearing, once again confirming Opinion No. 699-D and assuring Kansas and Kansas producers that *ad valorem* taxes could lawfully be passed through.

Shortly thereafter, Colorado Interstate Gas Company (Colorado Interstate) appealed the Northern decision to the Federal D.C. Circuit which, on June 28, 1988, held that FERC had not adequately explained its order. The case was remanded to FERC for clarification of how the Kansas *ad valorem* tax was similar to a production or severance tax under NGPA, Section 110. *Colorado Interstate Gas Co. v. FERC*, 850 F.2d 769,773 (D.C. Cir. 1988). The case sat idle on FERC's docket for a period of five years, from 1988 to 1993. This delay is significant because a subsequent FERC decision would cause interest claims amounting to millions of dollars to accrue during this period, through no fault of the producers.

Finally, in 1993, FERC issued an Order on Court Remand reversing Opinion 699-D and ordering refund of those taxes that had been included in the rates paid to Kansas producers after June 28, 1988, the date the Court of Appeals had first remanded the case to FERC. This ruling was appealed to the D.C. Circuit and in 1996, the Court found that Kansas' *ad valorem* tax did not qualify under NGPA, Section 110 and held that refunds would be due for taxes recovered commencing in October of 1983—expanding by five years the time period for which FERC had ordered refunds and exponentially increasing the claims of interest against Kansas producers and royalty owners! (October 1983 was when the notice of Northern's petition had been published in the *Federal Register*.) *Public Service Company of Colorado v. FERC*, 91 F.3d 1478 (D.C. Cir. 1996). By this decision, the D.C. Circuit essentially held all producers should have known that the challenge by Colorado Interstate in the Northern case would prevail. The Court went so far as to say the producers were "foolhardy" to think that they could have relied on a final non-appealable order of FERC, notwithstanding the administrative finality provisions of NGPA. FERC refused to waive interest, interpreting the Court's decision to require the imposition of interest on the principal obligation of the *ad valorem* tax refund.

During the next two years, various producers along with the State of Kansas, filed petitions and motions with FERC requesting relief from, and reconsideration of, its decision and additional relief in the form of waiver of interest on the principal obligation. In 1998, the Kansas Legislature passed Kansas Senate Concurrent Resolution No. 1616 stating that the

...retroactive reversal of a practice that had been legal for 19 years places an unjust and punitive financial burden, possibly exceeding \$500 million, on the Kansas natural gas industry, and that the ordered refunds threaten serious financial harm not only to Kansas natural gas industry but to the state and local economies and governmental budgets that rely on the industry's economic base...

and asked the U.S. Congress to provide relief from penalties and interest. Indeed, FERC has refused to grant any form of relief to Kansas and Kansas producers through either reconsideration of FERC's position regarding the retroactivity of its change of rule and policy or the waiver of claims of interest on those refunds. Nevertheless, FERC has required that 100% of the pipeline's claims be paid without hearing.

## POSITION OF KANSAS

I do not appear on behalf of the Kansas to allege that FERC should be precluded from changing its position regarding the definition of the "pass through" of *ad valorem* taxes or to challenge that authority. Clearly, such authority lies within the sound exercise of FERC's jurisdiction when applied on a prospective basis.

I appear here to object to the inequity which arises from that part of FERC's ruling which held that the refund obligation resulting from this policy reversal was retroactive! FERC's ruling, coupled with the controlling decision of the D.C. Circuit, has resulted in an overnight change of a policy which had been in effect for nineteen years! If this change were applied on a prospective basis only, I would not be here objecting. The D.C. Circuit Court contends that the producer's allegation of detrimental reliance on the nineteen years allowing the pass through of the *ad valorem* tax was "purely notional; if it were real it would not have been reasonable." Incredibly, how could the Court say it was not reasonable to rely on a 19-year history of consistent rulings by a federal regulatory agency? I agree something is not reasonable—but it was not the actions of natural gas producers! When Northern initially challenged the applicability of the ruling to Kansas' *ad valorem* tax, FERC said, in 1986, the pass through was "clear beyond question." How could the producers' action of relying on FERC's rulings be unreasonable when FERC itself continued to reaffirm them? Perhaps you could help me understand how to explain this to my constituents because I am absolutely at a loss as to how to do so. As my state's chief lawyer, I am unable to understand for myself and then explain to anyone else how our system of government and jurisprudence allows a 19-year ruling to be reversed overnight and be applied retroactively causing citizens to owe tens of millions of dollars in principal and interest.

What if the IRS were to reverse its prior decisions, although based on Congressional legislation, and rule that home mortgage interest payments are no longer deductible from income taxes—and not only are they not deductible on a prospective basis but taxpayers must now pay the amount of taxes they would have owed plus interest on that amount. Can you imagine the calls and letters your offices would receive over such an action? You have not heard the same level of outrage on this issue simply because it does not affect as many people. But I believe the situation with natural gas producers and royalty owners is equally as repugnant as my IRS scenario and producers and royalty owners are as deserving of protection and remedy from this Congress as would be homeowners.

The bills being sent to small natural gas producers have caused them to teeter on the brink of bankruptcy. Such adverse financial consequences, in a period of historic low prices, has spelled doom for the natural gas industry in my state. Not only do the owners, employees, and suppliers of the production companies suffer financially—the State of Kansas suffers as revenue from income, property, severance, *ad valorem*, conservation and anti-pollution taxes decline, including the income tax effects to the state of the refunds being ordered of major out of state producers.

The royalty owners are not the J.R. Ewings we remember from the television show, living in mansions and driving expensive automobiles. The royalty owners are retired farmers who have come to rely on the little "gas check" each quarter to supplement Social Security. The royalty owners are school teachers whose grandparents may have bequeathed them a  $\frac{1}{8}$  share of the gas well on the family farm. The royalty owners may be constituents of yours, not Kansas residents, who inherited or purchased an interest in a gas well in Kansas as a tax write-off. The bills the royalty owners are receiving are beyond the means of most of them and will ruin them financially. The interest the pipelines claim is due is now 160% of the principal!

And why are they being made to pay these exorbitant bills? Not because they were cheating on their taxes. Not because they hid their interest in a gas well from government officials. Not because they thought of a scheme to overcharge the pipelines and ultimately consumers, but because they were following the law as it had been interpreted consistently for 19 years by the agency!

Although it is the retroactive provision of the ruling itself that results in the present injustice and that I wish would be legislatively overturned, the Moran bill would at least provide a much needed remedy—albeit on a limited basis—to natural gas producers and royalty owners by making unlawful any interest or penalties assessed on those refunds. This bill will provide relief from the series of administrative and judicial decisions by FERC and the D.C. Circuit, respectively, which are manifestly unjust: decisions which penalize Kansas producers for complying with the law for 19 years; decisions which changed the rule and declared to be unlawful two decades of lawful actions of the producers; decisions which had called the legality of these very actions as "clear beyond question."



Under rules of FERC, no government agency is ever required to pay interest or penalties. Without remedy by Congress, the State of Kansas will owe a refund of the *ad valorem* tax that the Department of Parks and Wildlife passed through, although it will not owe interest. The elderly, widowed royalty owner will owe a refund of the taxes AND interest on the refund. What justifies this disparate treatment?

Under FERC's order, my great concern is that it is very likely that a large portion of the refunds and claimed interest will not flow through to the consumer. The second provision of House Bill 1117, which is just as important as the prohibition of claims of interest provision, would provide a protection to the consumer by requiring that all amounts refunded be passed through to the ultimate consumer.

I urge each of you to support this bill not just because it redresses such an unjust and detrimental effect on a significant sector of the Kansas economy: I urge you to support this bill in an effort to correct the effects of an unjust and unreasonable decision by an federal administrative agency against a sovereign state.

Mr. BARTON. Thank you, General. We would now like to hear from the gentlelady from Missouri, and I am sure she is going to exactly echo what the gentlelady from Kansas said.

Ms. Lumpe, you are recognized for 5 minutes.

#### STATEMENT OF SHEILA LUMPE

Ms. LUMPE. Thank you, Chairman Barton and members of the committee. As Chair of the Missouri Public Service Commission, I am speaking on behalf of them today.

And we thank you for the opportunity to present our testimony. I will not discuss the history in detail. I think it has been adequately presented. I would only like to reiterate that the issue did start in 1978 with the passage of the Natural Gas Policy Act.

This act outlined procedures and processes leading to the deregulation of the gas industry and in it Congress set ceiling prices. The refunds with interest from the unlawful collection of the *ad valorem* tax from 1988 to 1993 have been paid. However, no refunds have been given for the unlawful collection over the maximum legal price which consumers paid from 1978 to 1983.

The time of issue here are the years 1983 to 1988, and it was the U.S. Court of Appeals that required the refund go back to 1983. They did not go back further because that issue had not been raised.

The basic thought that we would like to leave with you is that consumers have been paying more than the maximum lawful price since the unlawful add on and passed through to them of the *ad valorem* tax. Our mission as commissioners under Missouri statutes is to provide adequate service at just and reasonable rates. The consumers have paid more than the just and reasonable price over that period of time. Our purpose is to see that they are refunded the money with interest to compensate them for the lost use of their money. The producers have had the use of these moneys, and we believe the consumers should have had the use of their moneys.

It is also important to note that the consumers have paid billions of dollars in transition costs over this period between 1978 and 1993 through take or pay contracts and gas supply realignment costs, approximately \$12 billion.

The second point is that the producers were on notice about this issue. As a matter of fact, it was a producer that first raised it by asking in 1983 that Texas receive the same treatment as Kansas. The fact that the case has dragged on so long also is not the fault

of the consumer. The parties demand due process. It is their right. And that takes time, and it is not unheard of for a party who may be benefiting from the status quo to wish to drag out a case as long as possible.

The producers, when they first filed their petition I am sure were sophisticated enough to know that they could lose, and a prudent business practice would have been to plan for such a contingency.

Third, we are not unsympathetic to the true hardship case of the small producers. However, we believe that each case has a unique set of facts and should be treated individually. We would not challenge hardship rulings where the information and the documentation are provided. Only if there appear to be significant discrepancies might we wish to take another look.

Chairman Barton, Congress passed the Natural Gas Policy Act in 1978. As I said, it is a carefully crafted piece of legislation. It balanced the rights of the different parties. It established procedures and processes that have worked well over a 20-year period. We oppose H.R. 1117 because it would violate those procedures and invite unpredictability and hosts of appeals on regulatory matters to Congress to solve.

We again thank you for the opportunity to appear before you. The Missouri Commission and its staff have worked long and hard to compile facts and information and we stand ready to assist you further in your deliberations.

Thank you.

Mr. BARTON. Thank you. Before we recognize Mr. Krehbiel, I want the gentlelady to know I got elected to Congress in 1984 on a platform of repealing the Natural Gas Policy Act of 1978. So I want you to know where I am coming from on this.

[The prepared statement of Shiela Lumpe follows:]

PREPARED STATEMENT OF SHEILA LUMPE, CHAIR, MISSOURI PUBLIC SERVICE COMMISSION

I. INTRODUCTION

Chairman Barton and Members of the House Subcommittee on Energy and Power, I am here today to testify on behalf of the Missouri Public Service Commission ("Missouri PSC"). The Missouri PSC is a governmental agency with jurisdiction to regulate the distribution and sale of natural gas to retail consumers in the state of Missouri. The Missouri PSC actively participates in Federal Energy Regulatory ("FERC") proceedings which affect the price of natural gas sold to local gas distribution companies located in Missouri.

Since 1989, the Missouri PSC has been on the front line with several other consumer advocates seeking recovery of the Kansas *ad valorem* refunds which are due to consumers in over 20 states. The Missouri PSC opposes H.R. 1117, because this bill seeks to relieve natural gas producers of their obligation to pay to natural gas consumers the accrued interest portion of *ad valorem* tax refunds related to the period 1983-1988.

As your invitation requested, I will address three areas: (1) the background of the *ad valorem* tax refunds, (2) the current status of the refund and interest payments, and (3) the pros and cons of the proposed legislation. I also wish to address several misconceptions that may exist on this matter.

II. BACKGROUND—KANSAS AD VALOREM TAX REFUNDS

By enacting the Natural Gas Policy Act of 1978 ("the NGPA" or the "Act") Congress established maximum lawful prices, or price ceilings, for first sales of natural gas. Section 110 of the NGPA provided for add-ons to the ceiling prices for state "severance or similar taxes" and for certain production costs. Section 504 of the Act made it unlawful for any person "to sell natural gas at a first sale price in excess

of any maximum lawful price under this Act.” The FERC, by regulation (18 C.F.R. § 273.301, attached as Exhibit A), imposed a refund obligation on any person, his successors, heirs and assigns who accepted a first sale price in excess of the maximum lawful price. FERC regulations also provide that refunds are to be paid with interest so that the recipient is made whole for the time value of money. NGPA Section—502(c) also permitted the FERC to make adjustments, “consistent with the purposes of the Act, as may be necessary to prevent special hardship, inequity or an unfair distribution of burdens.”

In 1983, a Texas producer petitioned the FERC to reverse a decision of the former Federal Power Commission (“FPC”), and to treat Texas *ad valorem* property taxes as a severance or similar tax under Section 110. Later that same year a pipeline asked the FERC to disallow Kansas *ad valorem* property taxes as a severance tax add-on under Section 110. By October 31, 1983, 21 Kansas producers and the Kansas Corporation Commission had intervened in the Kansas case.<sup>1</sup> In 1986 the FERC denied the petitions of both the Texas producers and the Kansas pipelines, keeping in place the disparate treatment of the Texas and Kansas property taxes under Section 110.

In 1988, the Court of Appeals remanded the matter to the FERC, saying the FERC had failed to provide a reasoned decision for treating the similar Kansas and Texas taxes differently. In 1993, the FERC concluded the Kansas *ad valorem* property tax did not qualify under Section 110 as a severance or similar tax eligible as an add-on to the maximum lawful price and that the collection of such *ad valorem* taxes on top of the ceiling prices caused the overall price of gas to exceed the maximum lawful level. The FERC ordered first sellers to refund only those amounts which were in excess of the maximum lawful price, and which were collected after the 1988 Court of Appeals decision.

On appeal of this 1993 FERC order, the Court of Appeals affirmed FERC’s treatment of the Kansas property taxes. The Court, however, reversed FERC’s holdings on the refund period and determined refunds were also owed dating back to 1983, when the challenge to the Kansas tax was first made and first sellers put on notice of the potential refund obligation. First sellers were allowed to retain all amounts collected in excess of maximum lawful prices from 1978 through 1983.

Since 1997 the FERC has issued a series of orders to effectuate the refunds to which consumers have a right under the NGPA. These orders are being challenged by both first sellers and consumers in more than a dozen cases currently pending before the Court of Appeals for the District of Columbia Circuit. In addition, parties have initiated more than one hundred cases before the FERC seeking adjustments or enforcement of refund obligations. [See Exhibit B.]

Under the structure of the NGPA and FERC practice, consumers have been required to pay the filed rates (which in this case have been excessively high) and rely on the FERC’s refund process to remedy the inequities. FERC did not require the disputed amounts of contested rates to be placed in escrow nor did it require that a bond be posted for later payment. However, the fact that first sellers did not voluntarily take any steps to notify their working and royalty interest owners and financially protect the disputed amounts from an adverse ruling in a pending case should not be a basis for denying ratepayers interest due on the amounts they were overcharged. Congress should not interfere with the process now, but instead preserve the equities.

In this respect, the Congress should be mindful that consumers have been forced to pay gas producers billions of dollars in take-or-pay and contract buyout costs. These costs were the result of the NGPA maximum lawful prices escalating above market clearing levels and resulting imbalances between supply and demand. Although consumer representatives requested the FERC and the courts to reform the high-priced producer contracts, no relief was forthcoming. Instead consumers were required to pay billions of dollars in take-or-pay and gas supply realignment costs to producers. [See Exhibit C.]

Much of the present turmoil springs from a later order in which the FERC announced that it would limit each first seller’s refund obligation to the extent of its working interest in the well from which the natural gas was sold and impose a di-

<sup>1</sup>The intervening parties supporting preferential treatment of the Kansas tax were: Arco Oil and Gas Co., Division of Atlantic Richfield Co.; Amoco Production Co.; Chevron U.S.A., Inc.; Maurice L. Brown Co.; Gulf Oil Corp.; Phillips Petroleum Co. and Phillips Oil Co.; Mobil Oil Corp. and Northern Natural Gas Producing Co.; Aminoil—Inc.; Champlin Petroleum Co.; Mesa Petroleum Co.; Pennzoil Co., Pennzoil Producing Co. and Pennzoil Oil and Gas, Inc.; Ashland Exploration, Inc.; Texaco Inc.; Kerr-McGee Corp.; Getty Oil Co.; Cities Service Oil and Gas Corps.; Shell Oil Co.; Sun Exploration and Production Co.; Kansas State Corporation Commission; Tenneco Oil Co.; Dorchester Gas Producing Co.; and, Cabot Petroleum Corp. *Sun Exploration and Production Co.* 36 FERC ¶61,093, Appendix B, (1986).

rect refund obligation on working and royalty interest owners. The Missouri Commission protested this FERC decision, and has asked the Court of Appeals to review it. The NGPA extended FERC jurisdiction *only* to first sales of natural gas. Since neither working interest owners nor royalty interest owners typically sell gas, the Missouri PSC believes this is a contract issue for the courts, not the FERC.

### III. CURRENT STATUS OF THE REFUND AND INTEREST PAYMENTS

According to the refund procedures prescribed by FERC, pipelines were directed to serve upon first sellers and file with the Commission a Statement of Refunds Due by November 10, 1997. First Sellers who collected revenues in excess of the applicable maximum lawful price as a result of the reimbursement of Kansas *ad valorem* taxes were to refund these excess revenues, with interest by March 9, 1998. FERC also explained that a first seller would be permitted to amortize the refunds over an extended period of time or be granted adjustment relief, if appropriate financial data was submitted to support such a request by an individual first seller. Additionally, FERC established a process through which disputes between first sellers and pipelines are to be resolved. First Sellers were allowed to place any disputed amounts into an escrow account, which would toll the interest obligation. FERC directed pipelines to flow through the refunds received to their customers who had been overcharged.

Nine pipelines filed Statements of Refunds Due in November 1997. These statements reflected a total of \$335 million Kansas *ad valorem* tax refunds due from producers. Of this amount, \$207.5 million, or 62%, was accrued interest. [See Exhibit D.] A review of the detailed information regarding the reported amounts due from 404 individual producers reveals the following information which we hope the Subcommittee will find useful in placing the various issues into perspective. [See Exhibit E.]

The first 24 producers owe 86% (\$288.4 of \$335 million) of the refunds.

- The total refund owed by each of those producers ranged from \$62.3 million to \$1.4 million.
- The amount of interest owed by each of those producers ranged from \$38.1 million to \$0.9 million.

The next 25 producers owe 7% (\$23.2 of \$335 million) of the refunds.

- Each owed less than \$1.4 million but more than \$0.5 million.
- Interest owed by each ranged from \$.9 million to \$0.3 million.

The remaining 355 producers owe 7% (\$23.4 of \$335 million) of the refunds.

- The total refund owed by each of those producers ranged from \$494,000 to less than \$100.
- The amount of interest owed by each of those producers ranged from \$311,000 to less than \$100.

Exhibit F summarizes the information contained in the pipeline annual refund reports filed in May of 1998 and May of 1999. The 1998 refund reports show that of the \$335 million owed, \$93.9 million had been paid by producers. The 1999 refund reports show that further amounts collected from producers during this second year are relatively small (\$3.1 million). Since interest continues to compound quarterly on any unpaid balances, the Missouri PSC prepared estimates of the additional interest that has accrued up through March 31, 1999.

There are no FERC filings that specifically show which states' consumers are owed or have received Kansas *ad valorem* tax refunds. Therefore the Missouri PSC applied a set of allocation factors that were developed from data contained in pipelines' 1983-1988 annual FERC Form—2 reports. [See Exhibit G.] Natural gas consumers in 23 states are entitled to Kansas *ad valorem* tax refunds owed. The Missouri PSC estimates that Kansas gas consumers are owed over \$80 million, with Missouri gas consumers being owed over \$60 million. Other states which are owed more than \$10 million are: Minnesota \$48 million, Nebraska \$37 million, Colorado \$24 million, Illinois \$23 million, Iowa \$20 million, Indiana \$17 million, and Michigan \$13 million.

The Missouri PSC has actively participated in FERC dockets related to refunds on the Williams and Panhandle pipeline systems and those court cases which affect the amount of refunds owed Missouri natural gas consumers.

### IV. CONS OF THE PROPOSAL TO WAIVE INTEREST

Consumers have been overcharged for natural gas dating back to 1983. Interest on the refunds is the means by which consumers are compensated for the time value of the money they were overcharged. It would be inequitable to deny consumers the interest to which they are entitled. It is equitable for producers to pay interest at

the FERC's refund interest rate for their use of these funds over the past 11-16 years.

The NGPA was a carefully crafted compromise of competing producer and consumer interests. The Act provided for the phased deregulation of various categories of new gas production while maintaining maximum lawful ceiling prices for sales of gas produced from older wells. By maintaining price ceilings on the older, flowing supplies of natural gas, Congress intended to temper the effect of deregulation of certain high cost gas through rolled-in pricing. To now allow producers to benefit from exceeding such maximum lawful prices, upsets the balance of producer and consumer interests reflected in the NGPA.

The issues of whether producers have overcharged consumers by collecting prices in excess of those established by Congress have been fully litigated at the FERC and affirmed by the Supreme Court. Issues associated with the interest on refunds are pending review before the United States Court of Appeals. Numerous petitions for adjustments and relief from refund obligations are currently being processed by FERC. It is unfair to disturb this regulatory and judicial process.

#### V. MISCONCEPTIONS

There is no basis to claims that producers were not provided notice of potential refund liabilities associated with their collection of Kansas *ad valorem* taxes from consumers. The large producers intervened in response to the public notice of FERC's review of this issue. These large producers have been involved throughout the entire regulatory and judicial process. Large first sellers and operators should have taken steps to insure that they could collect the contingent obligations from their working interest owners and royalty owners.

There is no basis to the claim that the harm to small producers can not be addressed absent a general waiver of interest. FERC is processing numerous requests for adjustment and relief from refund obligations, including interest, due to hardship. The Missouri PSC believes that relief should be permitted in cases where small producers demonstrate that the payment of refunds and interest will result in special hardship.

Reports of harm to the Kansas economy should be tempered by the fact that Kansas consumers are the single largest beneficiary of the refunds. As indicated in the Missouri PSC study, an estimated \$80 million in refunds will flow to Kansas consumers. The Kansas economy also has benefited from the millions of dollars gas supply transition costs paid by consumers to Kansas producers.

Reports have also surfaced that refunds are not flowing through to consumers. While there are several instances where pipeline customers have bargained away their rights to refunds, the vast majority of refunds will be flowed back to consumers pursuant to the authority of state utility commissions, such as the Missouri PSC. The issue of whether pipelines will flow through refunds to non-jurisdictional direct sales customers will generally depend upon contractual provisions relating to refunds. Direct sales customers are typically large industrial consumers who are capable of dealing with the pipeline directly.

#### VI. CONCLUSION

The Missouri PSC respectfully requests that Congress not interject itself into a regulatory and judicial process that is providing all affected parties the opportunity to pursue fair resolutions of difficult issues.

Thank you for the opportunity to appear before you today. I will be happy to answer any questions you may have. My staff is also available to assist you and provide any additional information you may need in your deliberations on this matter.

## Federal Energy Regulatory Commission

## § 273.302

## Subpart C—Refund Obligation

## § 273.301 General refund obligation.

The acceptance of a first sale price under this part by any person obligates such person, his successors, heirs, and assigns to refund any portion of any amount accepted which is in excess of the applicable maximum lawful price or the collection of which is not authorized by this subchapter, without regard to whether the seller has made a filing required by part 273 or has designated a person to make such filings on his behalf.

## § 273.302 Refunds of interim collections.

(a) *Applicability.* The provisions of this section apply to any interim collections made under the authority of subpart B of this part.

(b) *Refund obligations.* (1) Any interim collection under this part, whether made by a seller or any person designated by a seller pursuant to § 273.103(b), shall constitute a general undertaking to comply with the refund provisions of this subpart by the designee and any seller on whose behalf the collection is made.

(2) Additional refund assurance may be required at any time by order of the Commission.

(c) *Escrow.* For special rule applicable to escrow of amounts received during interim collections, see § 273.202(d)(3).

(d) *Records.* (1) If any interim collection is made under subpart B, for each billing period and for each purchaser the seller shall keep accurate accounts of:

(i) The price charged pursuant to subpart B of this part;

(ii) Resulting revenues as computed under the price being charged pursuant to this part;

(iii) The maximum lawful price that would have been applicable if interim collections under subpart B of this part had not been made;

(iv) The revenues that would have been collected under the maximum lawful price described in paragraph (d)(1)(iii) of this section; and

(v) The difference in revenues described in paragraphs (d)(1) (ii) and (iv) of this section.

(2) Such books and records shall be retained for a period of three (3) years after the termination of the interim collection period. Any contract under which any interim collections have occurred must be preserved for three (3) years after its expiration.

(e) *Refund payments.* (1)(i) Except as provided in paragraph (e)(1)(ii) of this section, within sixty (60) days after a determination becomes final denying a first sale eligibility for the price collected under this part, or within sixty (60) days after the date on which an application for determination is withdrawn by the applicant, while it is before the Commission or the jurisdictional agency, the seller must refund to the purchaser the refund amount computed under paragraph (h) of this section together with interest determined in accordance with §§ 154.102(c) and (d) of this chapter on the excess charges that have been collected from the date of payment until the date of refund.

(ii) If a refund required by paragraph (e)(1)(i) of this section is made through a billing adjustment, the seller and purchaser may agree that the billing adjustment will be completed in a reasonable period which may exceed sixty (60) days.

(iii) A purchaser may not use a billing adjustment to recover a refund required by paragraph (e)(1)(i) of this section before the expiration of the sixty (60) day period for the seller to make the refund unless the seller has previously agreed to the billing adjustment. If the seller fails to make a refund within the sixty (60) day period, the purchaser may use a billing adjustment to recover the refund without agreement by the seller. Before making a billing adjustment, a purchaser must provide the seller written notice of the amount of the refund to be recovered and the time period during which the billing adjustment will be completed.

(2) No interest is required to be paid on any portion of a refund:

(i) Which represents payments of royalties of taxes of Federal or State governmental authorities, except to the extent that such authorities pay interest to the seller when refunding overpayments of royalties or taxes; or

**Producer Ad Valorem Petitions Filed With FERC**

	Docket No.	MoPSC Intervention	Filer	Date Filed	Description
1	GP98-1		Union Pacific Resources	2/20/98	Offer of Settlement
2	GP98-2		Amoco Production Company	2/20/98	Offer of Settlement
3	GP98-3	X	OXY USA Inc.	2/20/98	Offer of Settlement
4	GP98-4	X	Amoco Production Company	2/20/98	Offer of Settlement
5	GP98-5		Mobil Oil Corporation	2/20/98	Offer of Settlement
6	GP98-6	X	Anadarko Petroleum	2/19/98	Offer of Settlement
7	GP98-7	X	OXY USA Inc.	2/23/98	Offer of Settlement
8	GP98-8		OXY USA Inc.	2/23/98	Offer of Settlement
9	GP98-9	X	Amoco Production Company	2/24/98	Offer of Settlement
10	GP98-10		Amoco Production Company	2/24/98	Offer of Settlement
11	GP98-11		OXY USA Inc.	2/24/98	Offer of Settlement
12	GP98-12		Amoco Production Company	2/24/98	Offer of Settlement
13	GP98-13	X	Mobil Oil Corporation	2/24/98	Offer of Settlement
14	GP98-14		Anadarko Petroleum	2/24/98	Offer of Settlement
15	GP98-15		OXY USA Inc.	2/24/98	Offer of Settlement
16	GP98-16	X	Union Pacific Resources	2/24/98	Offer of Settlement
17	GP98-17		Anadarko Petroleum	2/24/98	Offer of Settlement
18	GP98-18	X	Anadarko Petroleum	2/24/98	Offer of Settlement
19	GP98-19		Union Pacific Resources	2/24/98	Offer of Settlement
20	GP98-20		Union Pacific Resources	2/24/98	Offer of Settlement
21	GP98-21		Midgard Energy Company	3/6/98	Petition for Dispute Resolution
22	GP98-22		Kansas Natural Gas, Inc.	3/9/98	Petition for Dispute Resolution
23	GP98-23		LaJolla Properties, Inc.	3/9/98	Petition for Dispute Resolution
24	GP98-24		Bill C. Romig	3/4/98	Petition for Clarification
25	GP98-25		Plains Petroleum Company	3/9/98	Petition for Adjustment
26	GP98-26		Oneok Resources Company	3/12/98	Petition for Dispute Resolution
27	GP98-27	X	Oneok Resources Company	3/12/98	Petition for Dispute Resolution
28	GP98-28	X	Oneok Resources Company	3/12/98	Petition for Dispute Resolution
29	GP98-29		Oneok Resources Company	3/12/98	Petition for Dispute Resolution
30	GP98-30		Barbara J. Wilson, Inc./Rings of Saturn et al.	6/2/98	Petition for Dispute Resolution
31	GP98-31	X	Great Eastern Energy and Devel. Corp.	3/3/98	Petition for Dispute Resolution
32	GP98-32		Anadarko Petroleum	5/4/98	Complaint and Motion for Remand
33	GP98-33		Graham-Michaelis Corporation	5/19/98	Petition for Dispute Resolution
34	GP98-34		GP Exploration and Oil	5/20/98	Petition for Determination
35	GP98-35		Ethel Huffman McKee et al.	6/2/98	Petition for Dispute Resolution
36	GP98-36		Joyce A. Mims, Robert E. Mims, et al.	6/2/98	Petition for Dispute Resolution
37	GP98-37	X	James E. Silver	6/15/98	Petition for Clarification
38	GP98-38		Vastar Gas Marketing & Atlantic Richfield	7/7/98	Petition for Dispute Resolution
39	GP98-39		Finnery-Kearny County Gas Venture	7/7/98	Petition for Dispute Resolution
40	GP99-1		Mountain Petroleum-Corporation	12/23/98	Petition for Dispute Resolution
41	SA98-1	X	Bowers Drilling Company, Inc.	2/4/98	Petition for Adjustment
42	SA98-2	X	CLX Energy, Inc.	2/9/98	Petition for Adjustment
43	SA98-3	X	Edgar W. White	2/18/98	Petition for Adjustment
44	SA98-4		Edgar W. White	2/18/98	Petition for Adjustment
45	SA98-5	X	Edgar W. White	2/18/98	Petition for Adjustment
46	SA98-6	X	Wenert Trich	2/17/98	Petition for Adjustment
47	SA98-7	X	Dorchester Hugoton, Ltd.	3/2/98	Petition for Adjustment
48	SA98-8	X	Ensign Oil & Gas Inc.	3/2/98	Petition for Adjustment
49	SA98-9	X	Merleyn A. Calvin	3/2/98	Petition for Adjustment
50	SA98-10	X	Helmerich & Payne, Inc.	3/3/98	Petition for Adjustment
51	SA98-11	X	Mull Drilling Company, Inc.	3/5/98	Petition for Adjustment

## Producer Ad Valorem Petitions Filed With FERC

Docket No.	MoPSC Intervention	Filer	Date Filed	Description	
52	SA98-12	X	Estate of J. A. Mull, Jr.	3/5/98	Petition for Adjustment
53	SA98-13	X	Hoffmann Oil Company	3/6/98	Petition for Adjustment
54	SA98-14		Albert A. Thornbrough	3/6/98	Petition for Adjustment
55	SA98-15	X	Mark A. Gower	3/6/98	Petition for Adjustment
56	SA98-16		Midgard Energy Company	3/6/98	Petition for Adjustment
57	SA98-17	X	Midgard Energy Company	3/6/98	Petition for Adjustment
58	SA98-18		Riviera Drilling & Exploration	3/6/98	Petition for Adjustment
59	SA98-19	X	Dale Schwarzhoff	3/9/98	Petition for Adjustment
60	SA98-20		Dale Schwarzhoff	3/9/98	Petition for Adjustment
61	SA98-21	X	Sally L. Bone	3/9/98	Petition for Adjustment
62	SA98-22		Sally L. Bone	3/9/98	Petition for Adjustment
63	SA98-23	X	Raymond Oil Company, Inc.	3/9/98	Petition for Adjustment
64	SA98-24	X	Cabot Oil & Gas Corporation	3/9/98	Petition for Adjustment
65	SA98-25	X	Range Oil Company, Inc.	3/9/98	Petition for Adjustment
66	SA98-26	X	Glenn M. Dunne, Sr. Trust	3/9/98	Petition for Adjustment
67	SA98-27		Kaiser-Francis Oil Company	3/9/98	Petition for Adjustment
68	SA98-28		Kaiser-Francis Oil Company	3/9/98	Petition for Adjustment
69	SA98-29	X	Kaiser-Francis Oil Company	3/9/98	Petition for Adjustment
70	SA98-30	X	Kaiser-Francis Oil Company	3/9/98	Petition for Adjustment
71	SA98-31		Kaiser-Francis Oil Company	3/9/98	Petition for Adjustment
72	SA98-32	X	Devon Energy Corporation	3/9/98	Petition for Adjustment
73	SA98-33	X	Pioneer Natural Resources USA	3/9/98	Petition for Adjustment
74	SA98-34	X	McCoy Petroleum Corporation	3/9/98	Petition for Adjustment
75	SA98-35	X	Lee Banks d/b/a Banks Oil Company	3/9/98	Petition for Adjustment
76	SA98-36		George B. Angle d/b/a Frontier Oil Co.	3/9/98	Petition for Adjustment
77	SA98-37		Pickrell Drilling Company Inc.	3/9/98	Petition for Adjustment
78	SA98-38		John W. LeBosquet	3/9/98	Petition for Adjustment
79	SA98-39	X	Quinque Oil & Gas Producing	3/9/98	Petition for Adjustment
80	SA98-40		Hummon Corporation	3/9/98	Petition for Adjustment
81	SA98-41	X	Hummon Corporation	3/9/98	Petition for Adjustment
82	SA98-42		Leo Helzel	3/9/98	Petition for Adjustment
83	SA98-43	X	Leo Helzel	3/9/98	Petition for Adjustment
84	SA98-44	X	Molz Oil Company	3/9/98	Petition for Adjustment
85	SA98-45	X	Molz Oil Company	3/9/98	Petition for Adjustment
86	SA98-46		Quinque Operating Company	3/9/98	Petition for Adjustment
87	SA98-47	X	Quinque Operating Company	3/9/98	Petition for Adjustment
88	SA98-48		Graham-Michaelis Corporation	3/9/98	Petition for Adjustment
89	SA98-49		Graham-Michaelis Corporation	3/9/98	Petition for Adjustment
90	SA98-50	X	Graham-Michaelis Corporation	3/9/98	Petition for Adjustment
91	SA98-51		Kansas Petroleum Inc.	3/9/98	Petition for Adjustment
92	SA98-52		Kansas Petroleum Inc.	3/9/98	Petition for Adjustment
93	SA98-53		Kansas Petroleum Inc.	3/9/98	Petition for Adjustment
94	SA98-54	X	Lee Banks d/b/a Banks Oil Company	3/9/98	Petition for Adjustment
95	SA98-55		Lee Banks d/b/a Banks Oil Company	3/9/98	Petition for Adjustment
96	SA98-56		Benson Mineral Group, Inc.	3/9/98	Petition for Adjustment
97	SA98-57		Benson Mineral Group, Inc.	3/9/98	Petition for Adjustment
98	SA98-58	X	Benson Mineral Group, Inc.	3/9/98	Petition for Adjustment
99	SA98-59	X	Benson Mineral Group, Inc.	3/9/98	Petition for Adjustment
100	SA98-60	X	First National Oil, Inc.	3/5/98	Petition for Adjustment
101	SA98-61		Louis Weiner & Bruce Weiner	3/10/98	Petition for Adjustment
102	SA98-62		Ned E. & Dorothy J. Lowry	3/10/98	Petition for Adjustment



**Producer Ad Valorem Petitions Filed With FERC**

	<b>Docket No.</b>	<b>MoPSC Intervention</b>	<b>Filer</b>	<b>Date Filed</b>	<b>Description</b>
103	SA98-63	X	Mull Drilling Company, Inc.	3/10/98	Petition for Adjustment
104	SA98-64		R.J. Patrick Operating Company	3/10/98	Petition for Adjustment
105	SA98-65		Pickrell Drilling Company Inc.	3/10/98	Petition for Adjustment
106	SA98-66	X	R.J. Patrick Operating Company	3/10/98	Petition for Adjustment
107	SA98-67		John O. Farmer, Inc.	3/11/98	Petition for Adjustment
108	SA98-68		Mark A. Gower	3/11/98	Petition for Adjustment
109	SA98-69		Pickrell Drilling Company Inc.	3/10/98	Petition for Adjustment
110	SA98-70	X	Pickrell Drilling Company Inc.	3/10/98	Petition for Adjustment
111	SA98-71		Graham-Michaelis Corporation	3/10/98	Petition for Adjustment
112	SA98-72		John O. Farmer, Inc.	3/11/98	Petition for Adjustment
113	SA98-73	X	John O. Farmer, Inc.	3/11/98	Petition for Adjustment
114	SA98-74	X	George Grenyo	3/16/98	Petition for Adjustment
115	SA98-75		George Grenyo	3/16/98	Petition for Adjustment
116	SA98-76		Edwin A. Cornell	3/16/98	Petition for Adjustment
117	SA98-77		BP Exploration and Oil, Inc.	3/23/98	Petition for Adjustment
118	SA98-78		Total Minatome Corporation	3/25/98	Petition for Adjustment
119	SA98-79		Ruth Lawhorn	3/30/99	Petition for Adjustment
120	SA98-80	X	Hummon Corporation	4/3/98	Petition for Adjustment
121	SA98-81		Shannon Energy Corporation	4/7/98	Petition for Adjustment
122	SA98-82		Helmerich & Payne, Inc.	4/21/98	Petition for Adjustment
123	SA98-83		The Trees Oil Company	5/7/98	Petition for Adjustment
124	SA98-84		Inter-American Energy Corporation	6/16/98	Petition for Adjustment
125	SA98-85		Charles B. Wilson, Jr. et al.	6/15/98	Petition for Dispute Resolution
126	SA98-86		Beren Corporation	6/30/98	Petition for Dispute Resolution
127	SA98-87	X	Beren Corporation	6/30/98	Petition for Dispute Resolution
128	SA98-88		Beren Corporation	6/30/98	Petition for Dispute Resolution
129	SA98-89		Beren Corporation	6/30/98	Petition for Dispute Resolution
130	SA98-90	X	Beren Corporation	6/30/98	Petition for Dispute Resolution
131	SA98-91		Beren Corporation	6/30/98	Petition for Dispute Resolution
132	SA98-92		Broadhurst Operating	7/7/98	Petition for Adjustment
133	SA98-93		Eastman Dillon Oil & Gas	7/7/98	Petition for Adjustment
134	SA98-94	X	McGiness Oil Company	7/8/98	Petition for Dispute Resolution
135	SA98-95	X	Westmore Drilling Company	7/8/98	Petition for Dispute Resolution
136	SA98-96		IMC Global, Inc.	7/15/98	Petition for Dispute Resolution
137	SA98-97		IMC Global, Inc.	7/16/98	Petition for Dispute Resolution
138	SA98-98	X	IMC Global, Inc.	7/17/98	Petition for Dispute Resolution
139	SA98-99		IMC Global, Inc.	7/18/98	Petition for Dispute Resolution
140	SA98-100	X	IMC Global, Inc.	7/19/98	Petition for Dispute Resolution
141	SA98-101	X	Continental Energy	8/6/98	Petition for Adjustment
142	SA99-1	X	Burlington Resources Oil & Gas	10/30/98	Petition for Adjustment
143	SA99-2		Suerte Oil Company	11/2/98	Petition for Adjustment
144	SA99-3	X	John B. Fleeger, et al.	10/28/98	Petition for Adjustment
145	SA99-4		Questa Energy Corporation	11/4/98	Petition for Adjustment
146	SA99-5		Argent Energy, Inc.	11/5/98	Petition for Adjustment
147	SA99-6		Harken Energy Corporation	11/17/98	Petition for Adjustment
148	SA99-7	X	Charlotte Hill Gas Company	11/20/98	Petition for Adjustment
149	SA99-8	X	E.W. Dahlgren Trust	11/20/98	Petition for Adjustment
150	SA99-9	X	W.A.R. Gas Company	11/20/98	Petition for Adjustment
151	SA99-10		Burk Royalty Company	12/2/98	Petition for Adjustment
152	SA99-11	X	Alf M. Landon	2/9/99	Petition for Adjustment
153	SA99-12		Aladin Petroleum Corporation	1/11/99	Petition for Adjustment

Exhibit B

**Producer Ad Valorem Petitions Filed With FERC**

Docket No.	MoPSC Intervention	Filer	Date Filed	Description
154 SA99-13		Kaiser-Francis Oil Company	2/5/99	Petition for Adjustment
155 SA99-14	X	Green Wolf Oil Company	2/17/99	Petition for Adjustment
156 SA99-15		Vidor Pipeline Company	3/5/99	Petition for Adjustment
157 SA99-16		The Montana Power Company	3/19/99	Petition for Adjustment
158 SA99-17		Chevron U.S.A. Inc.	3/9/99	Petition for Adjustment
159 SA99-18		Chevron U.S.A. Inc.	3/11/99	Petition for Adjustment
160 SA99-19	X	Chevron U.S.A. Inc.	3/9/99	Petition for Adjustment
161 SA99-20		Chevron U.S.A. Inc.	3/10/99	Petition for Adjustment
162 SA99-21	X	Chevron U.S.A. Inc.	3/10/99	Petition for Adjustment
163 SA99-22		Atlantic Richfield Corporation	3/10/99	Petition for Adjustment
164 SA99-23		Atlantic Richfield Corporation	3/10/99	Petition for Adjustment
165 SA99-24	X	Atlantic Richfield Corporation	3/10/99	Petition for Adjustment
166 SA99-25		Texaco Exploration and Production	3/10/99	Petition for Adjustment
167 SA99-26		Texaco Exploration and Production	3/10/99	Petition for Adjustment
168 SA99-27	X	Texaco Exploration and Production	3/10/99	Petition for Adjustment
169 SA99-28	X	Texaco Exploration and Production	3/10/99	Petition for Adjustment
170 SA99-29		Texaco Exploration and Production	3/10/99	Petition for Adjustment

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Gas Supply Transition Costs

January 1997

Pipeline	TOP Costs Pre-636	TOP Costs Post 636	GSR Costs Less Dakota Costs
ANR	\$ 420,810,401	\$ 36,859,783	\$ 47,376,575
Arkla/NorAm	176,160,462	75,282,895	4,321,9762
CIG	39,413,710	6,085,935	0
CNG	26,417,960	461,054	0
Columbia	386,477,800	0	10,000,000
El Paso	1,496,828,811	13,586,634	0
Florida Gas	20,260,267	85,976,234	33,665,508
MRT	0	0	13,177,422
Natural	1,179,943,080	25,618,934	129,631,419
Northern	446,977,798	3,364,577	192,107,454
Northwest	154,482,899	1,074,895	0
Panhandle	406,242,382	2,931,228	14,977,294
PGT	0	168,475,392	14,977,294
Questar	3,331,315	0	0
Sea Robin	176,730,320	0	0
Southern	790,000,000	0	391,195,565
Tennessee	1,158,351,745	27,387,144	718,452,786
Texas Eastern	0	0	23,958,470
Texas Gas	178,281,575	3,384,199	49,718,965
Transco	1,097,544,715	0	0
Transwestern	249,702,151	33,276,523	0
Trunkline	410,688,415	0	893,624
Trunkline LNG	196,000,000	0	0
United/Koch	766,315,932	0	0
Valero	18,390,000	0	0
W. Texas Gath	3,433,376	0	0
Williams	60,223,873	0	65,409,351
Williston	43,733,000	28,702,928	14,370,226
	<b>\$9,906,741,987</b>	<b>\$512,468,355</b>	<b>\$1,709,256,621 = \$ 12,128,466,963</b>

\* PGT used the 500/528 recovery mechanism but made no distinction between TOP and GSR costs.

\*\* Staff estimate. Williams made no distinction between TOP and GSR costs.

\*\*\* This does not include amounts absorbed by TETCO in its settlement.

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**Summary of 1983-88 Kansas Ad Valorem Tax Reimbursements Due from First Sellers  
Principal plus Interest through 11/30/97 or 12/31/97  
Based upon Statement of Refunds Due filed by all Pipelines**

Pipeline	Principal	Interest	Total
Docket No: RP98-43 Anadarko Gathering Company	\$5,432,295	\$9,770,838	\$15,203,134
Docket No: RP98-42 ANR	\$409,903	\$777,829	\$1,187,732
Docket No: RP98-54 Colorado Interstate Gas Company	\$13,343,681	\$21,659,966	\$35,003,647
Docket No: RP98-44 El Paso Natural Gas Company	\$18,589	\$35,248	\$53,836
Docket No: RP98-53 KN Interstate GasTransmission Company	\$12,104,346	\$18,831,617	\$30,935,962
Docket No: RP98-38 Natural Gas Pipelines Company of America	\$84,412	\$155,254	\$239,666
Docket No: RP98-39 Northern Natural Gas Company	\$30,162,203	\$50,216,236	\$80,378,439
Docket No: RP98-40 Panhandle Eastern Pipe Line Company	\$20,000,859	\$33,594,414	\$53,595,273
Docket No: RP98-52 Williams Natural Gas Company	\$45,774,748	\$72,472,287	\$118,247,034
<b>TOTAL</b>	<b>\$127,331,034</b>	<b>\$207,513,689</b>	<b>\$334,844,723</b>

The Missouri PSC staff estimates that approximately 45-50% of the Williams Natural Gas refunds and 5-10% of the Panhandle Eastern refunds are due to Missouri natural gas consumer.

**Summary of 1983-88 Kansas Ad Valorem Tax Reimbursements Due from First Sellers  
Principal plus Interest through 11/30/97 or 12/31/97  
Based upon Statement of Refunds Due filed by all Pipelines**

First Sellers (in descending order by interest due)	Principal	Interest	Total
1 Amoco Production Company	\$24,207,052.89	\$38,100,733.73	\$62,307,786.62
2 Mobil Oil Corp	\$19,703,648.88	\$32,512,675.28	\$52,216,324.16
3 Oxy USA Inc.	\$11,758,538.02	\$18,572,234.61	\$30,330,772.63
4 Mesa Operating Limited Partnership	\$9,237,894.11	\$14,341,879.60	\$23,579,773.71
5 Anadarko Petroleum Corp	\$7,469,406.74	\$11,826,352.60	\$19,295,759.34
6 Helmerich & Payne	\$4,803,827.33	\$7,743,954.73	\$12,547,782.06
7 Pan Eastern Exploration Co	\$3,936,696.32	\$6,772,496.97	\$10,711,193.29
8 Barrett	\$4,449,459.79	\$5,963,694.58	\$10,413,154.37
9 Duke Energy Field Services	\$2,461,276.71	\$5,343,228.39	\$7,804,505.10
10 Mobil Natural Gas	\$2,995,694.20	\$5,282,814.60	\$8,278,508.80
11 Cities Service Oil & Gas Corp	\$2,650,251.11	\$4,620,195.21	\$7,270,446.32
12 Mesa Petroleum Co.	\$2,209,602.05	\$3,772,487.83	\$5,981,989.88
13 Osborne Heirs	\$1,895,174.57	\$3,533,602.54	\$5,428,777.11
14 Kansas Natural Gas Inc	\$1,521,183.50	\$2,710,357.69	\$4,231,541.19
15 Texaco Inc.	\$1,449,950.82	\$2,472,565.94	\$3,922,516.76
16 Energy Devel. Corp	\$1,555,736.48	\$2,400,622.07	\$3,956,358.55
17 Union Pacific Resources d/b/a Champlin Petroleum Co.	\$1,410,173.36	\$2,398,667.03	\$3,808,840.39
18 UPRC	\$1,359,526.80	\$2,347,098.64	\$3,706,625.44
19 Northern Pump Co	\$931,990.67	\$1,727,051.49	\$2,659,042.16
20 Union Pacific Resources	\$1,317,926.70	\$1,648,841.56	\$2,966,768.26
21 Petro-Lewis Corp	\$796,341.28	\$1,389,471.13	\$2,185,812.41
22 Beren Corp.	\$696,420.77	\$1,260,279.79	\$1,956,700.56
23 George A. Angle, D/B Frontier Oil Co.	\$500,863.36	\$941,653.07	\$1,442,516.43
24 Kuhn Drilling Co	\$476,947.92	\$937,186.59	\$1,414,134.51
25 Continental Energy	\$481,004.24	\$876,394.05	\$1,357,398.29
26 Champlin Petroleum Company	\$519,163.84	\$837,701.47	\$1,356,865.31
27 Hoi, FG	\$475,414.98	\$774,015.31	\$1,249,430.29
28 Chevron USA, Inc.	\$565,227.13	\$758,325.25	\$1,323,552.38
29 Kaiser-Francis Oi	\$447,110.28	\$734,663.83	\$1,181,774.11
30 Stevens County Oil & Gas Cc	\$380,640.26	\$729,343.05	\$1,109,983.31
31 APX Corp	\$604,751.57	\$711,759.41	\$1,316,510.98
32 McKelvy Operating Corp	\$458,726.64	\$700,658.34	\$1,159,384.98
33 Benson Mineral Group	\$354,759.27	\$676,761.77	\$1,031,521.04
34 Lebosquet, John R.	\$364,359.52	\$625,536.52	\$989,896.04
35 Southland Royalty Co	\$370,156.43	\$624,587.70	\$994,744.13
36 White, Robt. F.	\$346,374.92	\$613,182.29	\$959,557.21
37 Irex Corp	\$300,375.03	\$608,932.31	\$909,307.34
38 Graham Michaelis Corp.	\$383,708.92	\$569,907.35	\$953,616.27
39 Kansas Petro Inc.	\$343,662.84	\$562,506.35	\$906,169.19
40 Cabot Petroleum Corp.	\$365,451.23	\$528,777.73	\$894,228.96
41 Mapco Oil & Gas Company	\$207,510.69	\$442,789.97	\$650,300.66
42 Santa Fe Minerals Inc	\$308,134.36	\$425,699.33	\$733,833.69
43 Coastal Oil & Gas Corp.	\$234,052.27	\$391,903.59	\$625,955.86
44 Halliburton Oil Co.	\$200,029.17	\$385,051.19	\$585,080.36
45 Energy Exploration & Prod Inc	\$207,395.09	\$381,394.11	\$588,789.20
46 Arco Oil & Gas Co.	\$303,107.18	\$362,243.52	\$665,350.70
47 Lowry's Lease Management Inc.	\$240,082.66	\$358,049.16	\$598,131.82
48 Wilson, Robt. P.	\$196,013.39	\$326,326.50	\$524,339.89
49 Graham Michaelis Drilling Co	\$211,980.51	\$322,823.78	\$534,804.29
50 Marden Producing Co	\$180,316.01	\$311,547.21	\$491,863.22
51 Trees Oil Co	\$192,815.47	\$301,471.37	\$494,286.84
52 RJ Patrick Operating Co	\$139,143.93	\$297,482.32	\$436,626.25
53 Gould Oil	\$173,470.45	\$279,152.12	\$452,622.57
54 Upstream Energy, Service,CMY	\$171,409.21	\$278,439.99	\$449,849.20
55 Raymond Oil	\$130,246.58	\$245,888.20	\$376,134.78
56 Molz Oil	\$145,265.22	\$243,219.97	\$388,485.19
57 Petroleum Inc.	\$149,383.44	\$238,462.09	\$387,845.53
58 Dorchester Hugoton Ltd.	\$153,640.28	\$234,331.77	\$387,972.05
59 Muff Drilling Cc	\$159,178.16	\$229,005.86	\$388,184.02
60 Mid-Continent Energy Corp	\$112,843.96	\$216,630.02	\$329,473.98
61 Pickrell Drilling Cc	\$108,786.61	\$215,976.21	\$324,762.82
62 Green Wolf Oil Co.	\$120,119.66	\$210,634.47	\$330,754.13

**Summary of 1983-88 Kansas Ad Valorem Tax Reimbursements Due from First Sellers  
Principal plus Interest through 11/30/97 or 12/31/97  
Based upon Statement of Refunds Due filed by all Pipelines**

First Sellers (in descending order by Interest Due)	Principal	Interest	Total
63 UMC Petroleum Corporation	\$137,321.71	\$202,846.03	\$340,167.74
64 Service Drilling Company	\$100,611.67	\$202,586.66	\$303,198.33
65 Banks Oil Co	\$102,961.73	\$194,708.71	\$297,670.44
66 Kennedy & Mitchell	\$79,987.19	\$186,922.22	\$266,909.41
67 Burnett Corp	\$126,214.19	\$184,611.42	\$310,825.61
68 Gulf Oil Exploration & Production	\$95,481.46	\$181,881.00	\$277,362.46
69 Imperial Oil & Gas Inc	\$90,967.49	\$180,858.25	\$271,825.74
70 Goodland Gas Company	\$130,802.68	\$176,880.81	\$307,683.49
71 Intercep Resources Inc.	\$88,036.13	\$175,297.15	\$263,333.28
72 Calvin Exploration Inc	\$78,296.26	\$174,281.88	\$252,578.14
73 True Oil Co	\$85,207.81	\$169,839.61	\$255,047.42
74 Imperial Oil Cc	\$76,366.95	\$166,902.91	\$243,269.86
75 The Maurice L. Brown Co.	\$104,283.25	\$164,028.12	\$268,311.37
76 Inca Oil Corp	\$79,418.65	\$157,777.74	\$237,193.39
77 Thronbrough Albert A	\$108,883.73	\$156,621.88	\$265,505.61
78 Wilson Charles B Jr Inc.	\$98,528.47	\$154,333.42	\$252,861.89
79 Lear Petroleum Corp	\$83,030.63	\$151,739.86	\$234,770.49
80 Bowers Drilling Co	\$105,015.15	\$150,206.58	\$255,221.73
81 McKelvy, Alfred D	\$95,461.40	\$149,160.49	\$244,621.89
82 Kiwanda Energy Inc	\$117,798.02	\$139,437.62	\$257,235.64
83 Midguard Energy Company	\$66,629.35	\$134,109.65	\$200,739.00
84 Brock Resources	\$62,089.57	\$133,331.34	\$195,420.91
85 Gulf Oil Corp	\$103,015.54	\$121,435.76	\$224,451.30
86 Bristol Resources	\$74,519.63	\$120,082.19	\$194,601.82
87 Hinkle Oil Company	\$65,073.68	\$118,135.60	\$183,209.28
88 Hawkins Oil & Gas Inc	\$75,017.06	\$117,127.86	\$192,144.92
89 OneOk Exploration Co	\$72,795.12	\$115,413.48	\$188,208.60
90 Dorchester Gas Producing Company	\$56,725.47	\$115,326.19	\$172,051.66
91 Hummon Corp	\$61,686.11	\$115,306.92	\$176,993.03
92 Riviera Drilling & Explorator	\$68,857.97	\$114,418.86	\$183,276.83
93 Wallace Oil & Gas Inc	\$64,989.03	\$114,079.73	\$179,068.76
94 Clark Exploration	\$82,478.91	\$109,040.08	\$191,518.99
95 First National Oil Inc	\$74,763.95	\$107,403.88	\$182,167.83
96 Midwestern Exploration Co	\$55,759.71	\$107,332.56	\$163,092.27
97 Gear Petroleum	\$68,093.76	\$100,507.90	\$168,601.66
98 Matagorda Island Explorator	\$85,326.30	\$100,396.12	\$185,722.42
99 Par Petroleum Inc.	\$45,095.07	\$95,195.83	\$140,290.90
100 Forcenergy Onshore, Inc. (f/n/a Bow Valley Petrol	\$49,619.00	\$93,443.77	\$143,062.77
101 Burnaby Enterprises	\$60,143.90	\$92,545.84	\$152,689.74
102 Zenith Drilling Corp	\$48,573.81	\$89,958.65	\$138,532.46
103 White, Edgar	\$48,578.82	\$89,699.26	\$138,278.08
104 Benedum Trees Oil Co	\$52,881.57	\$89,635.16	\$142,516.73
105 Messman Rhinehart	\$53,689.76	\$87,151.19	\$140,840.95
106 Walter Kuhn Drilling Co.	\$45,411.63	\$85,885.32	\$131,296.95
107 Farmer, John O. Inc.	\$57,256.76	\$85,113.59	\$142,370.35
108 Hasada Industries	\$39,117.52	\$83,469.25	\$122,586.77
109 Tenneco Oil Co.	\$59,744.18	\$83,268.97	\$143,013.15
110 John P. Lockridge	\$41,603.40	\$80,810.03	\$122,413.43
111 White, Johnson	\$50,306.55	\$79,528.21	\$129,834.76
112 Bone, Sally L.	\$40,619.54	\$76,978.29	\$117,597.83
113 Sun Exploration & Prod Co	\$60,089.76	\$76,861.21	\$136,950.97
114 Kansas Natural Gas Inc., Hays KS	\$43,539.15	\$75,757.26	\$119,296.41
115 William A. Rookstool, Agent	\$47,079.71	\$73,965.95	\$121,045.66
116 Hugoton Energy	\$43,304.88	\$71,885.33	\$115,190.21
117 McMoran Oil & Gas Co	\$59,485.84	\$71,674.80	\$131,160.64
118 National Oil Company	\$36,666.09	\$71,233.16	\$107,899.25
119 Osborne, James L	\$39,874.25	\$70,686.29	\$110,560.54
120 Beymer & Beymer Inc	\$43,588.60	\$70,544.56	\$114,133.16
121 Oil Producers Inc.	\$36,442.31	\$68,296.84	\$104,739.15
122 J. T. Oil Co.	\$40,592.10	\$68,026.76	\$108,618.86
123 Horner, Richard	\$39,100.98	\$67,038.57	\$106,139.55
124 Petroleum Production	\$49,966.55	\$66,784.45	\$116,751.00

**Summary of 1983-98 Kansas Ad Valorem Tax Reimbursements Due from First Sellers  
Principal plus Interest through 11/30/97 or 12/31/97  
Based upon Statement of Refunds Due filed by all Pipelines**

<b>First Sellers in descending order by Interest Due</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
125 Banks, Lee	\$34,035.37	\$66,074.28	\$100,109.65
126 Trigg Drilling Company	\$30,290.16	\$65,784.57	\$96,074.73
127 Marathon Oil Co.	\$47,801.52	\$65,513.04	\$113,314.56
128 Osborne, W.B., Jr.	\$35,708.01	\$65,145.38	\$100,853.39
129 Williams Bros. Engineering	\$47,916.76	\$64,023.65	\$111,940.41
130 Hondo Oil & Gas Co	\$44,021.45	\$61,652.08	\$105,673.53
131 Inter-America Energy Corp.	\$35,771.02	\$61,593.65	\$97,364.67
132 Kaiser-Francis Operating Account	\$37,871.73	\$60,841.33	\$98,513.06
133 Cabot Oil & Gas	\$40,337.41	\$60,269.20	\$100,606.61
134 H.I. Inc.	\$32,031.07	\$60,093.55	\$92,124.62
135 Quinque Operating Co	\$29,715.24	\$58,477.42	\$88,192.66
136 Fina Oil & Chemical Co.	\$44,846.45	\$58,363.25	\$103,209.70
137 Ensign Oil & Gas Inc.	\$46,959.55	\$57,578.56	\$104,538.11
138 Elk Co. Gas Gathering System	\$33,804.70	\$57,075.77	\$90,880.47
139 Rider, Don C.	\$44,025.17	\$56,883.23	\$100,908.40
140 National Coop Refinery	\$32,957.83	\$56,436.47	\$89,394.30
141 Trich, Wenert	\$26,095.34	\$54,721.85	\$80,817.19
142 Kimbark Oil & Gas Company of Colc	\$32,308.62	\$53,014.98	\$85,323.60
143 Comanche Production Inc.	\$21,720.18	\$51,009.02	\$72,729.20
144 Olympic Petroleum Co	\$34,877.98	\$50,909.29	\$85,787.27
145 Williams, Robt. L. (f/n/a Imperial Oil & Gas, Inc.	\$24,299.87	\$49,938.64	\$74,238.51
146 Damson Oil Corp	\$31,813.07	\$49,912.90	\$81,725.97
147 La Jolla Properties, Inc.	\$22,244.71	\$49,110.51	\$71,355.22
148 Post Petroleum Co	\$26,315.09	\$48,903.25	\$75,218.34
149 Ozark Production Co Inc.	\$30,346.99	\$48,739.12	\$79,086.11
150 Petroleum Production Management Inc.	\$39,705.19	\$48,433.72	\$88,138.91
151 Reserve Pipeline, Inc., Operato	\$31,449.49	\$48,392.24	\$79,841.73
152 Cotton Petroleum Corp	\$24,223.06	\$46,800.69	\$71,023.75
153 Diamond Shamrock Explor Co	\$28,575.46	\$46,717.80	\$75,293.26
154 K & E Drilling Co.	\$25,254.26	\$46,381.40	\$71,635.66
155 Lange, RW	\$23,815.49	\$45,369.46	\$69,184.95
156 Gear, James R.	\$28,693.86	\$45,308.11	\$74,001.97
157 Dietrich Petroleum Corp	\$26,444.47	\$45,008.75	\$71,453.22
158 Kansas Gas Purchasing	\$24,742.17	\$44,603.30	\$69,345.47
159 Oleum Inc	\$22,688.15	\$44,253.21	\$66,941.36
160 Colonial Corp	\$23,233.39	\$43,981.39	\$67,214.78
161 Vincent Oil Corp	\$23,380.28	\$43,682.58	\$67,062.86
162 N.H. Wheelless Operating Acct	\$26,602.68	\$43,595.46	\$70,198.14
163 CIG Exploration	\$22,129.95	\$42,882.86	\$65,012.81
164 Tom F. Marsh Inc.	\$21,231.00	\$42,201.10	\$63,432.10
165 Suerte Oil Company	\$25,898.17	\$42,163.33	\$68,061.50
166 Jackson, Donald	\$20,199.34	\$40,845.44	\$61,044.78
167 Resources Exploration Ltd	\$25,210.67	\$40,765.17	\$65,975.84
168 Jones, George	\$26,419.73	\$40,356.02	\$66,775.75
169 Griggs Oil Inc.	\$24,284.24	\$39,781.91	\$64,066.15
170 Santa Fe Energy	\$25,227.31	\$38,898.80	\$64,126.11
171 Davies & Co. Inc.	\$19,338.37	\$37,118.46	\$56,456.83
172 Natural Gas Anadarko Inc.	\$19,689.43	\$36,602.74	\$56,292.17
173 Kaiser-Francis Oil d/b/a Lebon Oil Co	\$18,661.27	\$36,362.48	\$55,023.75
174 Loeb, Herman L.	\$29,330.70	\$35,651.54	\$64,982.24
175 Smith, Lester or Wanda	\$21,217.77	\$35,448.64	\$56,666.41
176 Vastar Gas Marketing	\$18,588.51	\$35,247.62	\$53,836.13
177 Smith E., III	\$19,346.34	\$33,574.06	\$52,920.40
178 Kimbark Oil & Gas Company	\$19,688.20	\$32,614.78	\$52,302.98
179 Decalta Intl. Corporation	\$18,137.31	\$31,302.06	\$49,439.37
180 Fina	\$23,590.98	\$30,793.42	\$54,384.40
181 Lowry Exploration	\$26,822.45	\$28,130.64	\$54,953.09
182 Hartman, WL	\$18,943.02	\$27,375.75	\$46,318.77
183 Johnson-Mizel Oil Co.	\$13,596.79	\$27,237.38	\$40,834.17
184 Murfin Drilling Company	\$20,490.10	\$27,061.97	\$47,552.07
185 Sterling Drilling Company	\$14,938.39	\$26,141.30	\$41,079.69
186 Koch Industries Inc.	\$15,616.29	\$24,744.21	\$40,360.50

**Summary of 1983-88 Kansas Ad Valorem Tax Reimbursements Due from First Sellers  
Principal plus Interest through 11/30/97 or 12/31/97  
Based upon Statement of Refunds Due filed by all Pipelines**

First Sellers (in descending order by interest due)	Principal	Interest	Total
187 Bangert, H.E.	\$16,280.52	\$24,091.94	\$40,372.46
188 Sunburst Exploration Co.	\$15,578.12	\$24,046.62	\$39,624.74
189 Santa Fe Androver Oil	\$16,303.84	\$23,999.05	\$40,302.89
190 Horseshoe Oper.	\$12,946.00	\$23,313.70	\$36,259.70
191 Maxus Energy	\$11,873.68	\$22,897.19	\$34,770.87
192 Barth, Jimmy C.	\$11,315.54	\$22,889.09	\$34,204.63
193 Barth, Max	\$11,315.54	\$22,889.09	\$34,204.63
194 Antares Oil Corp	\$12,486.95	\$21,721.66	\$34,208.61
195 Landon, Alf M.	\$11,899.52	\$21,045.11	\$32,944.63
196 Cox, Edwin L.	\$10,722.68	\$20,475.73	\$31,198.41
197 F&M Oil Company	\$9,205.24	\$18,890.12	\$28,095.36
198 Rice, Ruth	\$11,284.60	\$18,731.91	\$30,016.51
199 McGinness Oil Company	\$8,706.29	\$18,425.18	\$27,131.47
200 B&B Farm Industries, Inc.	\$8,342.41	\$18,117.89	\$26,460.30
201 Quinque Oil & Gas Producing	\$7,756.58	\$17,979.28	\$25,735.86
202 Okmar Oil Co	\$9,587.88	\$17,585.77	\$27,173.65
203 Mallonee Mchoney Inc.	\$12,073.34	\$17,426.53	\$29,499.87
204 Robinson Oil Company	\$13,271.45	\$17,073.78	\$30,345.23
205 Alpine Drilling Company	\$8,194.50	\$16,270.48	\$24,464.98
206 Multistate Oil Prop	\$7,963.55	\$14,531.45	\$22,495.00
207 Thompson Cattle Co.	\$8,652.85	\$14,385.42	\$23,038.27
208 Woolsey Petroleum Corporation	\$7,821.94	\$13,874.59	\$21,696.53
209 Ensource, Inc.	\$7,878.83	\$13,840.46	\$21,719.29
210 Knighton Oil, Company	\$9,566.88	\$13,818.25	\$23,385.13
211 Shaw, Geo R.	\$8,548.32	\$13,200.12	\$21,748.44
212 Helliar Drilling Co., Inc	\$6,350.37	\$12,701.34	\$19,051.71
213 Aurora Inc.	\$6,502.88	\$12,505.02	\$19,007.90
214 Powers, MF	\$6,901.44	\$12,200.55	\$19,101.99
215 Wilson, Barbara J	\$11,117.06	\$12,198.65	\$23,315.71
216 Cole Oil Co	\$8,159.30	\$11,671.62	\$19,830.92
217 Resource Tax Group	\$5,224.73	\$11,541.71	\$16,766.44
218 Union Valley Petroleum Corp	\$8,029.15	\$11,354.61	\$19,383.76
219 Exxon Corp	\$8,550.38	\$11,160.90	\$19,711.28
220 MH&M Joint Venture	\$8,322.61	\$11,145.27	\$19,467.88
221 Mims, Joyce A.	\$10,059.77	\$11,143.20	\$21,202.97
222 Barfield Oil Corp	\$7,265.34	\$10,775.83	\$18,041.17
223 Shannon, Bruce L.	\$8,931.32	\$10,569.85	\$17,501.17
224 Griggs Oil Company	\$4,666.96	\$10,543.44	\$15,210.40
225 Patton Oil Co	\$5,498.31	\$10,284.67	\$15,782.98
226 Mountain Petroleum Corp.	\$5,583.75	\$10,264.77	\$15,848.52
227 Vilas Oil & Gas	\$7,190.31	\$10,263.17	\$17,453.48
228 Stromquist, C. Dale	\$5,182.64	\$10,103.34	\$15,285.98
229 Rinehart/Chamberlain F Group	\$8,728.73	\$9,895.22	\$18,623.95
230 White, Hawk Oil Company	\$5,048.37	\$9,877.53	\$14,925.90
231 Burk Royalty	\$5,335.97	\$9,829.38	\$15,165.35
232 Bartle, Glenn G. (Estate)	\$8,161.39	\$9,605.51	\$17,766.90
233 Box, Harold E.	\$8,310.69	\$9,488.73	\$17,799.42
234 Martin Oil Producers	\$4,510.35	\$8,394.17	\$12,904.52
235 Hairford, John A.	\$4,784.02	\$8,184.77	\$12,968.79
236 Colony Energy Corp	\$4,967.13	\$8,014.33	\$12,981.46
237 Smith, MH	\$5,351.15	\$7,918.16	\$13,269.31
238 Hartman, W. L. Estate	\$5,211.16	\$7,752.40	\$12,963.56
239 Willis Gas Co	\$5,326.64	\$7,603.18	\$12,929.82
240 Martin Exploration Mgt	\$6,245.76	\$7,547.39	\$13,793.15
241 Harrington, Margaret E.	\$3,928.47	\$7,459.74	\$11,388.21
242 Beymer, Clyde Jr.	\$4,039.92	\$7,224.29	\$11,264.21
243 Plummer, Paul E.	\$5,562.16	\$7,133.93	\$12,696.09
244 Mapco Gas Products f/k/a MAPCA products	\$3,208.41	\$7,054.54	\$10,262.95
245 McCoy Petroleum Corp	\$4,327.18	\$7,015.33	\$11,342.51
246 Lunsz, Boston	\$4,326.50	\$6,980.38	\$11,306.88
247 Et Al, Inc	\$3,954.42	\$6,890.30	\$10,844.72
248 Excelsior Oil Corp	\$3,044.08	\$6,643.80	\$9,687.88



**Summary of 1983-88 Kansas Ad Valorem Tax Reimbursements Due from First Sellers  
Principal plus Interest through 11/30/97 or 12/31/97  
Based upon Statement of Refunds Due filed by all Pipelines**

First Sellers (in descending order of interest due)	Principal	Interest	Total
249 Kirkpatrick, WE	\$3,269.02	\$6,612.64	\$9,881.66
250 Walker, Myrl V.	\$3,296.03	\$6,047.05	\$9,343.08
251 Miller, Arthur R.	\$3,469.48	\$5,788.02	\$9,257.50
252 Marsh Operating Co	\$5,336.67	\$5,412.69	\$10,749.36
253 Romig, Bill C.	\$3,154.53	\$5,262.60	\$8,417.13
254 Energy Source Inc.	\$3,357.72	\$5,195.95	\$8,553.67
255 Short, Howard	\$2,612.29	\$5,054.78	\$7,667.07
256 Anadarko Production Company	\$2,516.88	\$4,872.59	\$7,389.47
257 Skinner, Hazel	\$2,844.48	\$4,598.39	\$7,442.87
258 Ingling, Donald	\$2,169.06	\$4,548.99	\$6,718.05
259 BH&K Company	\$2,285.91	\$4,445.90	\$6,731.81
260 Gulf Energy Pipeline Co.	\$2,278.15	\$4,364.87	\$6,643.02
261 Koehn, John W.	\$1,831.93	\$4,237.98	\$6,069.91
262 Lauck, DR	\$2,741.38	\$4,113.19	\$6,854.57
263 Summit Energy Inc	\$2,547.32	\$4,090.64	\$6,637.96
264 Enlow, Elmer A.	\$2,352.12	\$4,021.56	\$6,373.68
265 Walker, Val D.	\$2,032.83	\$3,900.53	\$5,933.36
266 Ives, Zelma	\$2,077.37	\$3,815.72	\$5,893.09
267 Lonita Inc.	\$2,545.82	\$3,789.87	\$6,335.69
268 CNG Producing Company	\$2,469.37	\$3,638.06	\$6,107.43
269 Freeman Russell F.	\$1,685.07	\$3,478.88	\$5,163.95
270 Jimmie V. & Lucille Iloai	\$1,904.00	\$3,443.95	\$5,347.95
271 Nadel & Gussman	\$2,066.74	\$3,422.54	\$5,489.28
272 Ensign Operating Company	\$2,655.36	\$3,291.86	\$5,947.22
273 Walker, Josephine	\$1,720.40	\$3,256.59	\$4,976.99
274 PC Ltd	\$2,477.67	\$3,234.12	\$5,711.79
275 American Petrofina	\$2,477.68	\$3,234.12	\$5,711.80
276 McLemore, Dean	\$1,803.32	\$3,207.93	\$5,011.25
277 The Rings of Saturn Inc.	\$2,915.98	\$3,127.03	\$6,043.01
278 Kornfeld, Jay	\$1,651.42	\$3,115.20	\$4,766.62
279 Pioneer Natl	\$1,576.36	\$3,034.68	\$4,611.04
280 Range Oil Co	\$1,305.70	\$2,968.94	\$4,274.64
281 Wilkonson, Lester	\$3,855.00	\$2,948.77	\$6,803.77
282 Shannon Energy Corp.	\$2,229.77	\$2,903.01	\$5,132.78
283 Messman Corp	\$1,365.11	\$2,849.90	\$4,215.01
284 Donovan, Pauline R.	\$1,689.22	\$2,830.42	\$4,519.64
285 Dutton, Ira V.	\$1,580.08	\$2,664.22	\$4,244.30
286 Ruth & Erwin H. Hanken	\$1,352.82	\$2,560.78	\$3,913.60
287 Finnup Foundation	\$1,622.59	\$2,555.00	\$4,177.59
288 Bowers, E.E.	\$1,952.31	\$2,528.63	\$4,480.94
289 Plains Petroleum Operating Company	\$1,600.63	\$2,436.41	\$4,037.04
290 H & J Production Co.	\$1,592.14	\$2,293.77	\$3,875.91
291 Hartman, W. L. Trust	\$1,745.05	\$2,292.42	\$4,037.47
292 Woods Petroleum Corp.	\$1,128.63	\$2,285.17	\$3,413.80
293 Crockett, Floyd	\$921.94	\$2,132.40	\$3,054.34
294 Getty Oil Co	\$1,162.44	\$2,125.17	\$3,287.61
295 JW Operating	\$1,272.73	\$2,087.82	\$3,360.55
296 Petroleum Energy Inc	\$1,083.74	\$2,075.17	\$3,158.91
297 Vincent, Ann W.	\$1,303.46	\$1,961.91	\$3,265.37
298 Robert G. Helm	\$1,106.93	\$1,956.19	\$3,063.12
299 Plains Petroleum Company	\$1,212.36	\$1,913.59	\$3,125.95
300 Kennedy, Howard (Trustee)	\$1,057.34	\$1,890.50	\$2,947.84
301 Judy Company	\$939.29	\$1,794.73	\$2,734.02
302 Flynn Energy Company	\$922.02	\$1,768.27	\$2,690.29
303 Isern Oil Co.	\$1,011.72	\$1,747.50	\$2,759.22
304 Fletcher, Frank	\$757.22	\$1,633.57	\$2,390.79
305 Rovenger, HM	\$860.01	\$1,581.00	\$2,441.01
306 Gilkison Paul D.	\$872.82	\$1,565.21	\$2,438.03
307 Beymer & Beymer	\$1,051.87	\$1,501.09	\$2,552.96
308 Kennedy Foundation	\$887.22	\$1,460.15	\$2,347.37
309 Dallas Production Inc.	\$809.18	\$1,449.11	\$2,258.29
310 Silver State Foundation	\$696.69	\$1,446.60	\$2,143.29

**Summary of 1983-88 Kansas Ad Valorem Tax Reimbursements Due from First Sellers**  
**Principal plus Interest through 11/30/97 or 12/31/97**  
**Based upon Statement of Refunds Due filed by all Pipelines**

First Sellers (in descending order by interest due)	Principal	Interest	Total
311 Bracken, Barth W.	\$858.89	\$1,427.21	\$2,286.10
312 Gladys J. Neuberburg	\$1,062.84	\$1,403.53	\$2,466.37
313 Francis J. Gillam	\$919.61	\$1,369.44	\$2,289.05
314 Ernest C. Mundhenke	\$811.10	\$1,361.67	\$2,172.77
315 Derley, Lloyd	\$777.70	\$1,345.68	\$2,123.38
316 Grant Oil, Inc.	\$669.25	\$1,342.13	\$2,011.38
317 Midway Operating Co.	\$646.66	\$1,307.04	\$1,953.70
318 Jackman, David Jr.	\$632.29	\$1,294.32	\$2,126.61
319 Hummon Oil Co	\$1,110.68	\$1,289.95	\$2,400.63
320 Dome Oil Corporation	\$507.48	\$1,275.85	\$1,783.33
321 Goodnight, Ollis	\$776.55	\$1,247.03	\$2,023.58
322 Veeder Supply & Dev Co	\$936.23	\$1,235.11	\$2,171.34
323 Zenith Natural Gas Co.	\$517.68	\$1,166.89	\$1,684.57
324 Steffen, Vern	\$690.11	\$1,151.29	\$1,841.40
325 Aylward Drilling Cc	\$561.02	\$1,090.86	\$1,651.88
326 Finnup, Isabel	\$637.29	\$1,090.69	\$1,727.98
327 Tucker, L. Scott	\$659.17	\$1,086.08	\$1,745.25
328 Box H.E	\$479.73	\$1,080.95	\$1,560.68
329 KBW Oil & Gas Company	\$456.03	\$1,017.20	\$1,473.23
330 L. J. & Helen Eddy	\$577.12	\$999.14	\$1,576.26
331 Pauline Suter	\$713.41	\$998.45	\$1,711.86
332 Rudd, Olive	\$585.84	\$965.26	\$1,551.10
333 Lowry Ned E.	\$429.37	\$965.21	\$1,394.58
334 Mitchell, John F.	\$424.39	\$961.04	\$1,385.43
335 BPSRR Enterprises	\$582.75	\$935.81	\$1,518.56
336 Howard and Joyce Cady	\$421.28	\$925.62	\$1,346.90
337 Draper, Paul A.	\$538.83	\$885.78	\$1,424.61
338 Van Vleet, Gerald T	\$483.38	\$881.01	\$1,364.39
339 Finnup, Frederick	\$530.59	\$852.12	\$1,382.71
340 Maddox, George	\$403.40	\$816.14	\$1,219.54
341 Oakwood Resources Inc	\$486.05	\$727.67	\$1,193.72
342 Texaco Producing Incs	\$367.62	\$836.58	\$1,074.20
343 Edward L. & Evelyn Juno	\$365.47	\$675.34	\$1,040.81
344 Halliburton Oil Co	\$319.23	\$660.86	\$980.09
345 Bianche Suter	\$474.43	\$637.20	\$1,111.63
346 Maxus Exploration Company	\$538.02	\$616.47	\$1,156.49
347 Rudd, S. Judson	\$365.72	\$610.12	\$975.84
348 McKee, RE & Jennie	\$560.73	\$596.87	\$1,157.60
349 Ruth Steffen	\$377.81	\$582.87	\$960.68
350 Kobs, Edwin	\$303.81	\$577.53	\$881.34
351 Texaco Exploration & Production	\$624.99	\$551.42	\$1,176.41
352 Allen, Sharon L.	\$314.59	\$549.58	\$864.17
353 McKee, Ethel Huffman	\$560.73	\$548.98	\$1,109.71
354 Elba Oil Cop	\$366.20	\$535.75	\$921.95
355 Boyd, John S.	\$221.43	\$505.65	\$727.08
356 Wilmar Oil Co.	\$371.83	\$486.90	\$860.73
357 A & L. Suter, Inc	\$348.16	\$482.63	\$830.79
358 Bill C. Roming	\$297.59	\$479.69	\$777.28
359 Donavan, Paul C.	\$261.84	\$434.52	\$696.36
360 Coppoc, Mary E.	\$245.12	\$413.30	\$658.42
361 Pickrell, Lloyd R.	\$159.29	\$366.46	\$527.75
362 J.C. Lemon Trust No. 1	\$327.33	\$364.75	\$692.08
363 Hernstadt, Wm. L.	\$236.30	\$359.92	\$596.22
364 Livingston Janet W.	\$145.08	\$327.60	\$472.68
365 Kuntz, William G.	\$184.30	\$317.52	\$501.82
366 Mace, Mervyn	\$164.82	\$314.42	\$479.24
367 Standley, John S.	\$185.87	\$314.36	\$500.23
368 Welte, Lillian A.	\$184.30	\$313.14	\$497.44
369 Wiler, Luella G.	\$184.10	\$309.58	\$493.68
370 Strain, Susie	\$184.30	\$309.07	\$493.37
371 Denton, Peggy D.	\$186.55	\$308.77	\$495.32
372 Boyd, Iona P.	\$175.03	\$295.12	\$470.15

**Summary of 1983-88 Kansas Ad Valorem Tax Reimbursements Due from First Sellers  
Principal plus Interest through 11/30/97 or 12/31/97  
Based upon Statement of Refunds Due filed by all Pipelines**

First Sellers (in descending order by amount due)	Principal	Interest	Total
373 Mims, Robt. E	\$265.35	\$291.43	\$556.78
374 JD Operating Co	\$129.79	\$289.50	\$419.29
375 Hasada Industries d/b/a Southwest Petroleum, Inc	\$137.93	\$279.69	\$417.62
376 Vance, Bert J.	\$239.34	\$270.94	\$510.28
377 Dome, Cecil G.	\$162.88	\$268.37	\$431.25
378 Brandes, Elma C.	\$147.99	\$248.87	\$396.86
379 Hall, Marcella	\$139.78	\$246.03	\$385.81
380 Wolfram, Almada	\$139.74	\$245.96	\$385.70
381 Riley, Imelda	\$139.74	\$245.96	\$385.70
382 Wolfram, Richard	\$139.78	\$235.69	\$375.47
383 Donovan, Edward R.	\$142.12	\$235.03	\$377.15
384 Phillips Petroleum Co.	\$134.74	\$218.37	\$353.11
385 Maddox, George F. & Co.	\$89.78	\$194.01	\$283.79
386 Hammcke, Leroy P.	\$112.16	\$187.11	\$299.27
387 Packer, Edna A. or RW	\$87.85	\$181.60	\$269.45
388 Appleman, Nate	\$82.71	\$172.06	\$254.77
389 Lowry Dorothy J.	\$70.21	\$157.77	\$227.98
390 Campbell Farm Agency	\$118.20	\$144.88	\$263.08
391 Brown Uriel	\$61.50	\$141.31	\$202.81
392 Mitchell Betty	\$62.21	\$138.86	\$201.07
393 Cottrell, JR	\$70.41	\$135.46	\$205.87
394 Mueller Oil Cc	\$106.91	\$121.02	\$227.93
395 Apolip Energies Inc.	\$78.77	\$119.98	\$198.75
396 Enertec Corp	\$53.13	\$91.97	\$145.10
397 Williamson, Marcia D.	\$53.78	\$82.10	\$135.88
398 Silver Slate Resources Corp.	\$48.68	\$53.46	\$102.14
399 Gielster, Lorine	\$14.64	\$25.34	\$39.98
400 Fitch, Venita F.	\$13.94	\$23.50	\$37.44
401 Kranenberg, Gene	\$13.24	\$22.92	\$36.16
402 Hawkins, John	\$18.58	\$21.09	\$39.67
403 Lock, Alvin	\$10.50	\$17.52	\$28.02
404 Petroleum Management Inc.	\$6.69	\$14.92	\$21.61
<b>TOTAL</b>	<b>\$127,391,834.46</b>	<b>\$207,213,688.58</b>	<b>\$334,605,523.04</b>

**SUMMARY OF ANNUAL PIPELINE REFUND REPORTS**

	Docket No.										Total
	RP98-43 Anadarko	RP98-42 ANR	RP98-54 CIG	RP98-44 El Paso	RP98-53 KNI	RP98-38 Natural	RP98-39 Northern	RP98-40 Panhandle	RP98-52 Williams		
<b>5/08 Reports</b>											
Payments Received	\$3,711,628	\$274,953	\$4,604,875	4/	\$5,028,711	\$183,209	\$36,287,555	\$7,587,115	\$36,177,074	\$93,855,121	
Non-jurisdictional Amounts	1/	1/	\$383,618	4/	\$3,047,268	1/	\$2,358,703	\$819,110	\$5,439,951		
Jurisdictional Amounts Distributed	1/	2/	\$4,221,257	4/	\$1,981,443	2/	\$33,929,074	\$6,773,185	\$30,737,123	\$77,842,092	
<b>5/99 Reports</b>											
Payments Received	\$0	\$309,326	\$435,724	4/	4/	4/	\$1,990,034	\$125,725	\$260,301	\$3,121,710	
Non-jurisdictional Amounts	1/	1/	\$36,299	4/	4/	4/	\$388,411	1/	\$39,975		
Jurisdictional Amounts Distributed	1/	3/	\$342,427	4/	4/	4/	\$1,613,710	\$0	\$0	\$1,956,137	

**Footnotes:**

- 1/ Information not available in report.
- 2/ Pipeline indicates the flow through of refunds to its jurisdictional customers should not be required in light of a FERC-approved settlement agreement with its customers.
- 3/ Pipeline indicates the FERC granted its request for waiver of the flowthrough of refunds to jurisdictional customers and reporting requirements
- 4/ No report filed

Exhibit G

<b>ESTIMATED ALLOCATION OF KANSAS AD VALOREM TAX REFUNDS (INCLUDING INTEREST) BY STATE AS OF MARCH 31, 1999</b>			
<b>#</b>	<b>STATE</b>	<b>ESTIMATED %</b>	<b>TOTAL REFUNDS DUE</b>
1	Kansas	22.556	\$60,466,040
2	Missouri	16.856	\$45,186,007
3	Minnesota	13.276	\$35,589,074
4	Nebraska	10.262	\$27,509,421
5	Colorado	6.567	\$17,604,207
6	Illinois	6.335	\$16,982,283
7	Iowa	5.460	\$14,636,663
8	Indiana	4.764	\$12,770,891
9	Michigan	3.534	\$9,473,621
10	Wisconsin	2.227	\$5,969,936
11	Ohio	1.754	\$4,701,961
12	California	1.581	\$4,238,199
13	Oklahoma	1.431	\$3,836,093
14	Texas	1.129	\$3,026,519
15	South Dakota	0.981	\$2,629,774
16	Wyoming	0.871	\$2,334,896
17	Arizona	0.242	\$648,731
18	New Mexico	0.061	\$163,523
19	Nevada	0.048	\$128,674
20	Louisiana	0.039	\$104,548
21	Arkansas	0.022	\$58,976
22	Utah	0.003	\$8,042
23	Tennessee	0.001	\$2,681
	<b>Total</b>	<b>100.00</b>	<b>\$362,968,627</b>

Mr. BARTON. Mr. Krehbiel is recognized for 5 minutes.

**STATEMENT OF ROBERT E. KREHBIEL**

Mr. KREHBIEL. Thank you Chairman Barton, members of the committee for the opportunity to testify. I am appearing today as an independent producer of natural gas in the State of Kansas and on behalf of an association of small independent oil and gas producers who work and operate in the oil and gas fields of Kansas.

Small independent producers are very important to energy in America and very important to energy consumers in America. They drill over 85 percent of all wells in the U.S. and account for 60 percent of gas production.

In Kansas, there are many small independent operators. They are small, family owned operations very similar to family farms. Many Kansas farmers, in fact, work in the oil fields and some operate their own small oil and gas companies to supplement depressed farm income.

But today while the U.S. economy flourishes, producers in both agriculture and oil and gas production are facing extraordinarily difficult economic times. Congressman Hall recognized the condition of the oil and gas industry in his opening statement. He was exactly correct.

The oil and gas producer was devastated by the crash in prices in the 1980's and has never recovered. For example, in the mid-1980's, there were over 220 rigs actively drilling for oil and gas in Kansas. Today there are three rigs running in Kansas. The value of oil and gas production in Kansas has declined by over \$1 billion annually and over 10,000 jobs in the producing sector alone have been lost.

Now the Kansas producer land owners are facing a new threat, the retroactive reversal of FERC policy. Producers are facing refunds totaling \$340 million resulting from gas sold to interstate pipelines from 10 to 15 years ago. Many years of good faith reliance and compliance with Federal policy has turned into a nightmare for many honest, hard working, and unsuspecting Kansas producers and royalty owners. I do not have expertise in FERC law and I am not here to discuss the legal issues. I simply want to share some producer stories with you which are typical of much of our membership.

For example, in February 1993, one young Kansas producer purchased 27 properties from a company that was being liquidated for the total sum of \$195,000. Ten of those properties were gas wells. In October 1998, this producer received a letter from the FERC telling him that he was liable for \$855,147, more than six times what he had paid for these properties. Both seller and buyer were without knowledge that any potential liability existed.

Many sales have occurred since 1983 to 1988, and this scenario will be repeated hundreds of times over. Innocent purchasers with no connection or relationship to the pipelines involved will be held liable for large sums of money which was paid to others.

Let me share the case of my good friend. In 1980, 19 years ago when the oil patch was booming, my good friend embarked on the American dream. He decided to raise some money and buy an oil and gas lease and drill a well. I worked with him to purchase an

oil and gas lease from a farmer on 160 acres in Edwards County, in Kansas.

He raised \$150,000 by selling interest to other producers in Kansas. He set up a corporation to operate the well and he provided the expertise and his wife did the book keeping. That is exactly the way the vast majority of wells are drilled in Kansas, by a group of producers coming together to share the costs of the risks of exploration. It is estimated that 5,000 independent producers sharing these costs and 50,000 royalty owners will be impacted by this decision.

Now, this group was successful in drilling the Edwards County well. They got a small gas well. A major interstate pipeline offered to buy the gas and they offered to pay the maximum lawful price set forth in the Natural Gas Policy of 1978.

And it is important to understand that never in the history of the gas patch has the independent producer charged a price for natural gas. Kansas producers, like Kansas farmers, are price takers, not price makers. To penalize a producer for charging a price in excess of the maximum lawful price when that price was set and determined by the purchaser and the government regulators is patently unfair and absurd on its face. To retroactively declare the conduct of innocent people unlawful is unconscionable.

With respect to the taxes, the attorneys in that contract said that the purchaser would reimburse seller for ad valorem taxes as provided in FPC opinion 699-D issued October 9, 1974. In reliance upon this language written by attorneys for the gas purchaser who referenced a valid order of the FPC, my friend signed this pipeline contract.

Fifteen years after signing this contract, a D.C. Circuit Court would say, as we see the issue, the apparent lack of detrimental reliance on the part of the producer is the crucial point. What would they have done differently if they had known in 1983 that they were not entitled to recover the tax?

Clearly the operator relied on Opinion 699-D when he signed that gas contract and accepted reimbursements for taxes. He was simply not in court to tell the judge that. The answer to the judge's query was simple. He would not have sold the gas or collected the tax. On November 4, 1996, my friend died never knowing that this case even existed. My friend's widow could not handle the operations. She sold the production and dissolved the corporation. One year later my friend's widow received a letter from the FERC referencing a FERC order dated September 10. This was the first knowledge that they had that this issue even existed.

In a letter dated November 18, 1997, to her old partners, to her husband's old partners, five of whom are now dead or dissolved, who shared the cost of this well, she described this as a big shock to all of us. Indeed it was. By the time that operator or any non-operator, first had notice that this issue even existed, FERC had already generated an interest penalty which was early twice as much as the principal.

Now the pipelines have gone to court to try to overturn another FERC decision. Previously FERC required the working interest owners only to be responsible for their share of the refund. Now they are trying to get the operator to be responsible for everybody's

interest. What that means is this widow will now be responsible for the share of the taxes of the five deceased partners in this well.

Mr. BARTON. Mr. Krehbiel, I know it is important that you get your comments on the record, but we have them in writing. If you could summarize in the next minute or so, we would appreciate it.

Mr. KREHBIEL. Thank you very much, Mr. Chairman. This issue should simply not exist. Thousands of innocent hardworking productive people who rely on and comply with Federal rules and regulations should not be penalized for the mistakes of Federal regulators.

This situation is not the fault of Kansas producers. These producers have served the American consumer with hard work and productivity. Common sense and equity demands fairness for producers as well as consumers. A healthy independent producing sector is in the best interest of all Americans.

Today that producing sector is rapidly being dismantled in the State of Kansas. Fairness in government regulations is critical. We urge you and appreciate your serious consideration of this issue. Thank you.

[The prepared statement of Robert E. Krehbiel follows:]

PREPARED STATEMENT OF ROBERT E. KREHBIEL, ON BEHALF OF THE KANSAS  
INDEPENDENT OIL AND GAS ASSOCIATION

Chairman Barton and members of the Subcommittee: Thank you for the opportunity to testify. I am appearing today as an independent producer of natural gas in the State of Kansas and as the Executive Vice-President of the Kansas Independent Oil and Gas Association. This association was organized over 63 years ago to provide a voice for the many small independent oil and gas producers who work and operate in the oil and gas fields of Kansas. We are a cooperating association of the Independent Petroleum Association of America.

There are 7,000 independent producers in America who typically employ 10 full time and 3 part time employees. They drill over 85% of all wells in the United States and account for 43% of oil production and 60% of gas production. In Kansas there are approximately 2,500 independent producers many of which are very small, family owned operations very similar to family farms. Many Kansas farmers work in the oil fields and some operate their own small oil and gas companies to supplement depressed farm income. Many working and retired farmers rely on royalty income resulting from production on their farm land.

Along with agriculture and manufacturing, the oil and gas industry has been a mainstay of the Kansas economy for many years. But today, while the U.S. economy flourishes, producers in both agriculture and oil and gas production are facing extraordinarily difficult economic conditions.

The independent oil and gas producer was devastated by the crash in prices in the mid 1980's and has never recovered. In the mid 1980's over 220 rigs were actively drilling for oil and gas in Kansas. Today, 3 rigs are running in Kansas. The value of oil and gas production in Kansas has declined by over \$1 billion annually and over 10,000 jobs in the producing sector alone have been lost. The attached Kansas Report reflects the most recent trends in the industry. Today, in Kansas, the average oil well produces only 2.4 barrels of oil per day. The average Kansas gas well produces less than 100 mcf of gas per day. Still, thousands of these marginally economic wells across America provide an enormous national resource. America still produces nearly half of the oil it consumes and ranks second to Saudi Arabia in world oil production. One Kansas stripper oil well making ten barrels of oil per day or stripper gas well making 90 mcf per day provides enough fuel to supply the needs of 150 Americans. Today, however, many of the stripper wells in Kansas do not provide enough revenue for producers to continue their operations.

Now, the Kansas producers and landowners are facing a new threat, the retroactive reversal of Federal Energy Regulatory Commission policy. After 19 years of reliance on Federal Power Commission Opinion 699-D by the State of Kansas and Kansas producers, the Federal Energy Regulatory Commission, successor to the FPC, reversed its opinion and ordered producers to pay the major inter state pipeline purchasers refunds totaling \$334 million resulting from the sale of gas produced



in Kansas and sold to interstate pipelines between October 3, 1983 and June 28, 1988. Approximately two-thirds of this amount is interest. It is estimated that just under \$100 million of this amount is demanded of small independent producers. Many years of good faith reliance on federal policy has turned into a nightmare for many unsuspecting Kansas producers.

This retroactive reversal of federal policy has created a series of legal issues which are infinite and complex. I understand that lawyers with expertise in these matters have identified issues ranging from complex constitutional questions to simple questions of private contract. New issues arise continually both at the federal and state level. Lawyers should fare very well. Some independent operators have pooled their resources to share the costs of counsel. Many of the small independent operators, non-operators and royalty owners in Kansas, however, lack the financial resources to employ skilled counsel. These producers do not, however, need legal advice to feel the outrage of the injustice of this federal regulatory action.

I do not have expertise in FERC law and I am not here to discuss the legal issues. I want to simply share one producer's story which is typical of much of our membership. The factual situation which I will discuss is true and, while it is not my purpose to discuss legal issues, many will appear. These issues are typical of what many Kansas producers are facing.

In 1980, nineteen years ago when the oil patch was booming, my good friend, a petroleum engineer with whom I had worked for several years, decided to raise some money, buy an oil and gas lease and drill a well. He was an honest, hard-working, productive man of utmost integrity. He was good at his work and well respected by those who knew him. He organized a corporation and, as a landman, I worked with him to purchase an oil and gas lease from a farmer on 160 acres in Edwards County, Kansas. He raised \$150,000 by selling interests in an exploratory well to ten friends or acquaintances with experience in the oil and gas industry. The corporation would operate the well with my friend providing the expertise and his wife doing the bookkeeping.

*The vast majority of exploratory wells drilled in Kansas are drilled by groups of individuals and companies who pool their resources to share the costs and risks of this very risky business. Behind every small operator is a group of non-operating working interest owners with substantial interests in the well.*

This group was successful in drilling the Edwards County well. By the end of 1980 they had completed a small gas well. It appeared that it would be good enough to recover their investment and possibly make some money. One major interstate pipeline company had a pipeline nearby as did several other gas purchasers. This pipeline offered to buy the gas and by January, 1981, their attorneys had written a Gas Purchase Contract. Sales commenced in March of 1981. Since the purchaser was an interstate pipeline their contract provided that they would pay the maximum lawful price as set forth in the Natural Gas Policy Act of 1978.

*Until deregulation, the maximum lawful price of gas sold in interstate commerce was always determined by the Federal Power Commission, or its successor the Federal Energy Regulatory Commission. In an unregulated market the price of gas is determined by the markets created by the pipelines. Never in the history of the gas patch has the independent producer "charged" a price for the natural gas he produces.* Kansas producers, like Kansas farmers, are price takers, not price makers. To penalize a producer for charging a price in excess of the maximum lawful price when that price was set and determined by the purchaser and government regulators is patently unfair and absurd on its face. To retroactively declare the conduct of innocent people unlawful is unconscionable. I understand the lawyers will also argue that it is unconstitutional.

The attorneys who wrote this gas purchase contract included a provision with respect to taxes, which read: "Purchaser shall reimburse Seller for all existing and new production, gathering, delivery, sales, severance, excise or other taxes or assessments of a similar nature including ad valorem taxes as provided in FPC Opinion No. 699-D, issued October 9, 1974." Under Opinion 699-D under specific ruling of the FPC, the Kansas ad valorem taxes could be added on to what otherwise was the maximum lawful price and could be re-imbursed as a part of the maximum lawful price. This ruling was later re-affirmed by the FPC's successor, the Federal Energy Regulatory Commission on at least two occasions in 1986 and 1987. In 1986 the FERC wrote that "it is clear beyond question" that the Kansas ad valorem tax can be paid to producers as part of their costs, and reaffirmed Opinion 699-D. Kansas producers relied on that opinion. Later, in 1993, nineteen years after the opinion was issued, and declared to be "clear beyond question", the Federal Energy Regulatory Commission reversed this opinion.

*In reliance upon this language written by Attorney's for the gas purchaser who referenced a valid order of the Federal Power Commission, Opinion 699-D, my friend*

*signed the Pipe Line's contract as president of the corporation, and acted in accordance with its terms.*

Fifteen years later on August 2, 1996, in an effort by the Pipe Lines to overturn Opinion 699-D, in the case of Public Service Company of Colorado, et al., Petitioners v. Federal Energy Regulatory Commission, Respondent, OXY USA, Inc. et al., Interveners, United States District Court of Appeals, District of Columbia Circuit, Judge Ruth Bader Ginsburg would write for the Court: "As we see the issue, the apparent lack of detrimental reliance on the part of the producers (on Opinion 699-D) is the crucial point. What would they have done differently if they had known in 1983 that they were not entitled to recover the Kansas tax?" Clearly the operator did rely on Opinion 699-D when he signed the gas contract and accepted re-imbursment for taxes. He was simply not in court to tell the judge that. The answer to the Judge's query was simple, they would not have sold the gas or collected the tax re-imbursments. Seller had no idea this case even existed. Had he been timely notified of this case he would have had the opportunity to tell the Judge that he would not have signed that gas purchase contract. Instead the Court ordered producers to refund any ad valorem taxes paid by the gas purchaser pursuant to Opinion 699-D back to October, 1983, "the date when all interested parties were given notice in the Federal Register that the recoverability of the Kansas tax under Sec. 110 of the NGPA was at issue." This operator did not subscribe to the federal register. Neither did his partners. Later the FERC would triple the refund by adding interest at high rates compounded quarterly.

On November 4, 1996, my friend died, never knowing that the Public Service Company of Colorado case even existed. My friend's widow could not handle the operations without the help of her husband and shortly after his death she sold their production and dissolved the corporation.

On November 10, 1997, the Pipe Line sent the widow a letter addressed to the now dissolved corporation which referenced an Order of the Federal Energy Regulatory Commission dated September 10, 1997. A copy of that letter is attached. This was the first knowledge that she had that this issue even existed. In a letter dated November 18, 1997, to the old partners, five of whom were now dead or dissolved, who had shared the costs and risks of drilling an exploratory well, the widow described the letter from the Pipe Line as "a big shock to all of us". *By the time that the operator or any non-operator first had notice that this issue even existed, FERC had already generated an interest penalty which was nearly twice as much as the principal.* In the case of this group the principal was \$6,502.88 and the interest was \$12,505.02, for a total liability at that time of \$19,007.90. It is very likely that even to this day many non-operating interests their heirs, successors or assigns and hundreds of royalty owners have no idea that this case even exists. Neither does the completely unknowing purchaser of this depleted property have any idea of the potential liability he purchased. The Edwards County farmer from who I purchased the oil and gas lease is deceased and his children have no idea of their potential liability. *It appears that if the pipeline cannot collect from the decedent they will attempt to collect from the decedent's widow and children. If the pipeline cannot collect from the widow and children they will attempt to collect from the unknowing purchaser.* Efforts to extend the jurisdiction of the FERC over persons and property stretch the imagination. The litigation that will be generated from these efforts will extend through the next decade.

In this case the Pipe Line purchased gas in accordance with the terms of their Gas Purchase Contract dated January 15, 1981, and had complied with FPC Opinion 699-D by reimbursing the producer for the ad valorem taxes that the corporation had paid to Edwards County for tax years 1983, 1984, and 1985. Even though the term of the contract was for a period of 15 years, the Pipe Line determined that the gas market had declined and they could buy the gas for a lesser price. Northern notified the corporation that they would no longer take gas from the Edwards County well and essentially voided the contract. Unable to operate without cash flow and unable to market the gas from a well which is now greatly depleted, the operator had little choice but to sign an amended agreement. Effective October, 1986, the Pipe Line reduced the price paid for natural gas from a then maximum lawful price of \$3.22 to approximately \$1.81 per mcf. Ad Valorem taxes paid to Edwards County were no longer refunded. By August of 1987, the Pipe Line, knowing that the well was greatly depleted and that no other purchaser would be willing to lay a pipeline to the wellhead to purchase the remaining reserves offered to pay \$1.18 per mcf. On August 29, 1987, the operator wrote to his working interest owners to tell them that the well would be shut in. A copy of that letter is attached.

*For the period of time for which refunds are set out in the Colorado Public Service Company opinion, October 1983 through June of 1988, the period of the alleged overpayments, the Pipe Line actually paid these producers an estimated \$49,000.00 less*

than the maximum lawful price allowed by the Natural Gas Policy Act of 1978, even with the refund of ad valorem taxes in 1983, 1984 and 1985. I understand that this is a typical scenario. Are producers supposed to suffer the losses of a weak market while the government eliminates the benefits of a good market? Can producers be required to refund monies alleged to have been collected in excess of the maximum lawful price when they were actually paid much less than the maximum lawful price during this period of time? Were consumers not the beneficiaries of this price reduction? Doesn't equity cry out?

In looking at my friend's scenario you also see a series of contractual issues arise which have never been considered, or should be reconsidered, by the FERC in ordering refunds. For example, on January 15, 1985, the Pipe Line proposed an amendment to the gas purchase contract to continue purchasing gas at a reduced price. That amendment included a provision which stated that Pipe Line would never be required to pay seller a price in excess of the maximum lawful price established by the FERC... and Seller agrees to promptly refund any excess payments made by Northern including interest calculated at the prime rate in effect at the Chase Manhattan Bank." Seller would not agree to this proposal because it required the payment of interest on some possible retroactive refund. With hindsight it becomes apparent that by this time the Pipe Line attorneys knew that Opinion 699-D had been challenged and if successful they wanted to get producers contractually responsible to refund interest on any principal recovery which might result. My friend would not agree to that and any refund of interest was stricken from the contract. Clearly, and equitably, in view of the price reduction accepted, any responsibility for a FERC ordered payment of interest on a retroactive refund should be the contractual responsibility of the purchaser.

Finally on January 14, 1994, producer and purchaser entered into a Termination Agreement discharging each other from any and all liabilities, claims and causes of action, whether known or not, arising out of or relating to said contracts between the parties. Typically, under these agreements, and the new gas purchase agreements entered into concurrently with them, in addition to agreeing to price reductions the producer releases claims which it could assert and which would add to the cost of the purchaser. The consideration for the producer's release is the release of possible claims against it. Clearly a pipeline and a producer should be able to agree between themselves as a matter of contract to indemnify and hold the other harmless from cross claims and liabilities including any refund obligations. The purchaser would not enter into the contract or mutual release unless it was receiving sufficient consideration, and it is the best judge of this. In this situation the pipeline is acting in the best interests of the consumer, as it is entering into the contract to reduce its costs. In fairness and under its power to make equitable adjustments, FERC should honor the mutual release and require no refund from either the producer or pipeline, as the consumer has already received the benefit of the producer release by reduced costs. Requiring a refund from the producer while retaining the benefits of the producer release and revised contract is a double burden and inequitable. The producer then pays twice, once by the release and price reduction, and secondly by the refund.

*Issues of private contract such as these have not been considered on an equitable basis and are plentiful. If these issues cannot be resolved en masse the Kansas courts will abound in litigation for years to come.*

Now, I understand, the Pipe Lines are asking the Washington, D.C. Circuit Court to have another order of the FERC overturned. This order stated that producers would only be liable for their own working interest, which order has been reaffirmed on several occasions. The FERC order holds producers responsible for their own working interest only. The Pipe Lines would have the Court require the operator to be liable for the interest of all working interest owners. In other words, the Pipe Lines would have the Court require my friend's widow to refund the interests of all of her husbands old partners. If she cannot recover her partner's shares because they are deceased, missing or bankrupt she will be forced to suffer their loss. The fairness of that will be difficult to explain to her. It should be difficult to explain to anyone.

While the dollars involved in this case are small, these situations repeat themselves over and over amongst Kansas producers and the impact on the people involved is significant. For many the cost of defense will surely exceed the amount at issue. But the impact goes beyond the money. Never have I seen an issue strike a nerve of honest, hardworking productive people in such a manner. It generated a sense of injustice among innocent people that was most accurately described by one state senator as "the worst taxation atrocity ever perpetrated by a federal agency" and it serves to generate a feeling of hostility. This should not be.

Personal stories abound in an industry that has been devastated by tough economic conditions. One geologist, whom I will call Bill, who lost the benefits of many years work in the last price crash and now works for \$2,500 per month, will receive an order to refund \$8,775 to one major pipe line purchaser. Another elderly Kansas producer, who lost many of his assets in the last crash and now lives on social security, will receive an order to refund \$12,000. The heirs of a deceased geologist may well be required to refund \$4,000. Before the Colorado Public Service case was decided or anyone had knowledge of it, one innocent purchaser bought a good amount of production which, during the period from 1983 to 1988, had been sold to an interstate pipe line. He was later aghast to learn that the FERC would order him to refund \$267,000 to a pipe line he had never been affiliated with.

These issue should not exist. Thousands of innocent, hardworking, productive people, who rely on and comply with federal rules and regulations should not be penalized for the mistakes of federal regulators. These producers have served the American consumer with hard work and productivity. Common sense and equity demands fairness for producers as well as consumers. A healthy independent producing sector is in the best interests of all Americans, producers and consumers alike. Fairness in government regulation is critical to a free society. We urge you to address this serious issue.

Mr. BARTON. Thank you, sir.

We would now like to hear from Mr. Majeroni.

#### STATEMENT OF JOHN MAJERONI

Mr. MAJERONI. Thank you, Mr. Chairman.

When you saw that a royalty owner was going to be here, you probably didn't expect to see someone from an eastern university talking about something from Kansas. But the royalty owners, people affected by this are really all over the country. This is a large field. It has been in existence for a long time. I bet there are people in every one of your districts who are royalty owners in this field.

The average royalty owner that I know of isn't a big rich person or producer thereof. When I go to Kansas to the annual meetings, they are farmers and ranchers and pretty common people. A lot of them are elderly, and they look on these royalty checks sort of like a supplemental security system. But there are also not-for profits like Cornell. There are local school districts and churches and others. We think this is really unfair to the royalty owners who are a very affected party by all this.

Mr. BARTON. Is Cornell a royalty owner?

Mr. MAJERONI. We are a royalty owner in the field, a large royalty owner, yes. We already talked about the flip-flops and the decisionmaking at FERC. I really don't want to comment any more about that. But it is important to know that the royalty owners really have no control. The nature of the lease is such that we don't dictate where wells are drilled if they are drilled.

We have nothing to do with who the gas is sold to or what price is paid. We didn't direct the taxes to be paid. In most instances, the taxes weren't even sent to the royalty owners. They go right to the producers who pay them or else passed them on to the pipeline companies to pay them directly.

For certain, the royalty owners have had absolutely no control, no decisionmaking in what has occurred over the last 15 years. Most royalty owners aren't even aware of the situation to my knowledge. There may have been a newsletter from an association or something in the newspaper, but it is the kind of thing you read and in the back of your mind you don't understand; you just think that doesn't affect me.

If there was a mistake made, we feel that the royalty owners shouldn't have to pay for it, especially true with interest. We have yet to be billed. Most of us, including Cornell University, have received no bills from anybody, and yet the interest continues to accumulate. And we really have nothing to say about it and don't even have an understanding of the scope of what we would owe.

Three, royalty owners were already in a less than equitable financial position and should not be punished further. The term of an oil and gas lease is very long. Most of these leases are 40 or 50 or 60 years long and when the bargains were struck in the 1930's and 1940's, one-eighth was a fair take for a royalty owner. If you do a lease today, it is 20 or 25 percent. So the royalty owners are already sort of on the short end of the stick financially and we think to push this off on them just sort of punishes them further.

Four, the intent of the interest here is really punitive. If interest is part of a financial transaction, if I am going to buy an expensive television set, I can make a decision. Do I wait or is the interest worth it for me to borrow the money and have it now. The other form of interest is a punishment. And clearly that is the case here. We are being punished. It is being tacked on because the producers should have known better, but the royalty owners had nothing to say about this, not involved in the decision, yet we are also being punished.

We didn't ask to pay the money. Many of us haven't been given opportunities to pay it back, but the interest clock continues to tick. And I think just by looking at the facts of \$130 million of the original debt and \$210 million in interest shows that it is really intended to be punitive. FERC mentioned that if there is no interest, then they lose the time value of money, but one of the earlier speakers said the average consumer is looking at \$15 so it is the difference between \$6 or \$7 for a consumer, \$15, it is just not a big difference to the consumer, I don't think.

The fifth reason is that in many cases those who have benefited 15 years ago are not the same as the people who are going to be punished now. Properties have been sold; parents have passed away. There have been divorces. How does this money get collected? So in the end, the collection is bound to be uneven and equitable. And the producers recognize this, and this is one of the reasons why they are not anxious to take on this burden of trying to collect from the royalty owners because they know what kind of a hassle and how unequitable this is going to be.

Last, as was mentioned before, there are no real winners here; but there are plenty of real losers. I too wonder if this is all going to go to the consumers, why are the pipeline companies fighting so hard for this. I have a feeling that some of it is going to end up staying with them. I think I know why some of the States are fighting hard for it too and some of the commissions. I think they see this as going in their pocket, but it is a real and painful impact to royalty owners.

I got a phone call over the weekend from someone who knew I was going to be here, a Kimberly Nicholson who lives in Vancouver, Washington, a royalty owner. Her mother had these royalties for years. Kimberly, her mother, passed away a couple of months ago from Lou Gehrig's disease and these royalties took care

of her mom. In March, Kimberly got a bill from a producer saying you owe \$25,000 due in 10 days just out of the blue.

You know the people who live in your districts. They can't pay a \$5,000 bill out of the blue let alone a \$25,000. This is the impact it is having. Something should be done to provide for the royalty owners. We think the bill waiving the interest is a very good step in the right direction.

[The prepared statement of John Majeroni follows:]

PREPARED STATEMENT OF JOHN MAJERONI, CORNELL UNIVERSITY REAL ESTATE DEPARTMENT, ON BEHALF OF THE SOUTHWEST KANSAS ROYALTY OWNERS ASSOCIATION

#### INTRODUCTION

My name is John Majeroni of Ithaca, New York. I'm a West Point graduate from the Class of 1974. During my six years in the Army I served as a Platoon Leader, on General Staff, and as a Company Commander. Shortly after getting out of the Service I went to work for Cornell University and am now the Director of the University's Real Estate Department. I have been managing Cornell's oil and gas properties for 18 years. I am not an attorney. I think I represent a knowledgeable, but lay-person's, point of view.

I was invited to speak by the Southwest Kansas Royalty Owners Association (SWKROA)—a non-profit Kansas corporation, organized in 1948 to protect the rights of landowners in the Hugoton Gas Field. Cornell is a member of this organization which has a membership of around 2,500 members, many of whom are farmers and ranchers. Most of its members are family owners of mineral interests, as distinguished from the companies that act as producers, operators, or working interest owners. SWKROA has been our primary source of information about the ad valorem tax refund problem. In fact, to my knowledge, we've had no communications from our producers or the FERC on this very important issue.

You may be surprised to see a representative from a university here. I'm probably not what you expected to see. When you think of a royalty owner, perhaps you have visions of rich Texans, like "J. R. Ewing". But the impact of the ad valorem tax refund issue is much greater than a few rich oil men. It impacts thousands of people and organizations who own mineral and royalty interests, including not-for-profit organizations, such as Cornell University. It impacts local school districts and churches.

The average royalty owner isn't rich. They are farmers and ranchers. In many instances these royalty and mineral interests have descended from generation to generation from people who lived in Southwest Kansas many years ago. Current royalty owners often only own a small fraction of the original interest. Many of the royalty owners are elderly. These royalty checks are like their Social Security supplements. Further, this is not an issue which affects only Kansas residents. Persons throughout the United States and several foreign countries own these minerals and are affected by this ruling. It is certain that some royalty owners are among your constituents.

And so my remarks are being made on behalf of all affected royalty owners to seek legislative relief from the impact of the Federal Energy Regulatory Commission (FERC) order dated September 10, 1997. In that ruling, FERC ordered first sellers of natural gas to make refunds of reimbursement for Kansas ad valorem taxes paid from 1983 to 1988, plus interest, including reimbursements attributable to royalty interest owners.

I am here because of the unfair and unjust treatment which FERC has inflicted upon the royalty owners. Apparently it is legal, but it is wrong.

It is wrong because people are being punished for flip-flops in decision making at FERC. It is wrong because royalty owners had, and continue to have, absolutely no control over any decisions relating to the issue, and yet we bear not equal, but even more liability, than those who have control. It is wrong because royalty owners are already in a less-than-equitable position financially in most wells and are only being punished further. It is wrong because the nature of the compound interest calculations on the amount due makes it punitive. It is wrong because in many cases, those who benefited will not be the same as those who are being punished. And it is wrong because there will be no real winners, but plenty of real losers—in other words: the action will be an unearned windfall of profits for pipeline companies, but will have a substantial, painful impact on the royalty owners from whom it is being

collected. And besides arguments of equity, there are still legal questions relating to FERC's jurisdiction over royalty owners and the statute of limitations. I'd like to go briefly into detail on each of these issues.

*Flip-Flops In Decisions At FERC.*

FERC itself created the problem by first determining that the Kansas ad valorem taxes could be passed through to pipeline companies, and then later changing its mind, thus creating the problem that royalty owners presently face.

Several years prior to the passage of the Natural Gas Policy Act of 1978, the Federal Power Commission (FPC), (the predecessor of the Federal Energy Regulatory Commission (FERC)), had held that producers could increase the applicable just and reasonable rate for natural gas to recover "state production, severance or similar taxes", and that any state ad valorem tax "based on production factors" was a "similar tax" which could be added to the national rate. In 1976, the FPC held that the Kansas ad valorem tax qualified because the bulk of the tax was based upon production factors.

In 1978, the Natural Gas Policy Act ("NGPA") set maximum lawful prices for the first sale of various categories of natural gas. Under Section 110(a)(1) of the NGPA, the first sale was allowed to exceed the maximum lawful price to the extent necessary to receive "state severance taxes attributable to the production of such natural gas." The NGPA defined "state severance tax," as "any severance, production, or similar tax, fee or other levy imposed on the production of natural gas."

Oil and gas producers in Kansas, relying on FPC and FERC rules, "passed through" the Kansas ad valorem taxes to consumers of natural gas. The time frame covered by the controversial ad valorem tax refund is for the years 1983 through 1988.

The problem arose when FERC changed its position some fifteen years after its order and retroactively ruled that the producers should not have been allowed to pass the Kansas ad valorem taxes through the pipeline companies to the consumers.

FERC then ordered producers (first sellers) to reimburse the consumers, through the pipeline companies, for not only the ad valorem tax which had been added to the maximum lawful price, but also for interest. FERC has also attempted to exert control over Kansas royalty owners by urging the producers to collect the refund from royalty owners, taking the position the producer will be liable to also pay the royalty owner's share of the refund *with interest*.

The projected impact of the FERC's unfair decision is estimated to be approximately \$340 million dollars. Of this amount, approximately \$200 million dollars represents interest. Congressman Moran has introduced a bill to waive the interest portion of refund obligation. This would be a significant help, but Congress should go further by overruling FERC's September 10, 1997 and subsequent orders.

Kansas State Senator Stephen R. Morris, R-Hugoton, made an analogy that FERC's actions should evoke a similar reaction that taxpayers would make if the Internal Revenue Service (IRS) were to disallow the deduction of home mortgage interest, with no justification, and require taxpayers—who had been relying on regulations which the IRS had been operating under for twenty or more years—to retroactively pay back the amount of the home mortgage deduction, plus interest. Surely, such action would raise a public outcry of illegal, unfair and unjust treatment by a federal agency. Yet FERC, if left unchecked by Congress, has caused such a travesty.

*Royalty Owners Had No Control.*

The way that a gas lease is structured, royalty owners have no control over the wells. We don't control when or where the wells are drilled. We don't control the price gas is sold for, or to whom the gas is sold. We certainly don't control expenses of drillers. We didn't direct taxes to be paid on our behalf. In most instances, royalty owners didn't even see the tax bills. Generally, the taxes were billed by the County Treasurer directly to the producer who either paid the taxes, including the royalty share, and then sought reimbursement from the pipeline companies for the taxes. Or, the producer billed the pipeline company for the taxes and the pipeline company paid the taxes.

For certain, we have had absolutely no decision making in this issue. None. In most cases, royalty owners don't even have any knowledge or aren't aware that there is an issue. If there was as mistake, royalty owners shouldn't pay for it. This is especially true of having to pay interest. Most royalty owners have yet to be billed (or even notified), and yet interest continues to grow and compound!

Despite this lack of control over any decisions relating to the ad valorem issue, we bear not equal, but even more liability, than those who did have control. Because of the way that ad valorem taxes are determined, royalty owners generally pay more

than 1/8th of the amount that producers pay because they have no effective deductions to offset against the tax as do the producers, such as depreciation. (One-eighth (1/8) is the normal fraction for royalty paid under old oil and gas leases.) SWKROA has estimated the ad valorem tax bill for royalty owners could be in the range of 20 to 30 percent of the total ad valorem assessment rather than the usual 1/8th. Based on that estimate, Kansas royalty owners could potentially be asked to refund between 68 to 100 million dollars. That, of course, is a huge amount by anyone's standards.

*Royalty Owners Were Already In A Less-Than-Equitable Position Financially.*

The FERC ruling is also wrong because it is seeking to "adjust" a position that was inequitable to begin with. Prices for Hugoton gas in the 1983-1988 time frame were capped at unrealistic levels of \$.50 per MCF or less. Pipeline companies were already profiting at royalty owners' expense. The FERC ruling essentially directs us to pay over even more profit for the pipeline companies. The leases from which the affected mineral owners are receiving royalties, are for a long term, most of them being fifty to sixty years old. Most of these leases provide for 1/8th royalty. This is already unfair to landowners since new leases are at 20-25% royalty. Why punish the royalty owners further?

*The Interest Calculations On The Amount Due Make It Punitive.*

Interest is fair and proper if knowledgeable financial transactions are entered into. Decisions are made about whether or not "the interest" is worth the advanced funds. This is the decision one makes when deciding to buy an expensive TV on credit or save for it. In this instance, royalty owners had no opportunity to make any decision on the payment of interest.

The interest assessed by FERC isn't part of a financial transaction. It's a form of punishment—a punishment for an act taken by somebody else, not the royalty owner's. FERC arbitrarily assigned interest to accrue. To my knowledge, there has been no judicial determination that interest should be charged.

The FERC interest rates also appear to be very high, especially by today's standards. We didn't ask to borrow the money. We haven't been asked yet to repay it. The interest continues to accrue and we don't even have information on what we supposedly owe. This is patently unfair.

Further, the typical royalty owner certainly did not earn the level of interest being charged. They spent it. They live on it. Interest is bad enough, but compound interest is particularly punitive. Someone once said "interest never sleeps." It is certainly true in this case. Look at the facts here: \$140 million owed, \$200 million in interest.

*Those Who Benefitted Will Not Be The Same As Those Who Are Being Punished.*

The funds in question are 10 to 15 years old. In some cases properties have been sold. In other cases, parents have passed away. How are these funds to be collected?

Royalty owners who inherited minerals subsequent to 1988 are not subject to the refund claim under the *Wylee* case. Different producers are approaching the problem in different ways. Imagine, in your district, going back and trying to collect an adjustment in taxes that was levied on homeowners 15 years ago. Imagine the confusion as you try to sort out who was living where when and who should pay.

Collection is bound to be uneven and inequitable. The producers even recognize this and, as you will see by their statements in subsequent pages, object to being put in the position of collecting these funds.

SWKROA Director John Crump, in 1998, testified before the Kansas Legislature in support of Kansas Senate Bill No. 685 (which later became HB2419) and gave several reasons for supporting SB685. Among his arguments was that collecting this debt would be difficult, expensive and time-consuming for the producers to locate and correspond with those royalty owners who owned the royalty interests from 1983 to 1988. Crump then pointed out examples of the inconsistencies in the pattern of billing by some of the producers on the claimed refunds.

*There Are No Real Winners, But Plenty Of Real Losers.*

There are really no injured parties in the FERC ruling, but enforcing the ruling will certainly injure plenty of people. Who is the money going to? While the ultimate destination of the funds to be collected is not clear, you must also ask why are the pipeline companies fighting this issue so hard. Is it to benefit the consumers who should receive the recoupment? Or is it more likely that the pipeline companies will keep it?

The action will be an unearned windfall of profits for pipeline companies who, remember, are already reaping more than their fair share of profits.



If efforts are made to somehow distribute the funds to all natural gas users in America, it will provide no meaningful benefit to their lives. It may end up getting distributed to them in the form of grocery coupons or it might end up as a one-time deduction of a few cents off their gas bill. However, there is a real, substantial, painful impact on the royalty owners from whom it is being collected. Imagine the typical family in your district getting a bill in the mail for \$5,000, or \$25,000, or \$100,000. They simply don't have the savings to pay it. Some of the producers are signaling that if payments aren't made, they will just stop making royalty payments and collect it that way. But if royalties stop, it will still be have huge impact on royalty owners, many of whom are elderly. They've adjusted their lives to live off of it. In some cases, for generations.

Let me give you an example of the impact. I recently spoke on the phone with Kimberly Nicholson. She lives in Vancouver, Washington. Her family owns minerals in Kansas. They are a moderate family with three children and an average income. She was also caring for her mother, who lived nearby in a small two room house. Her mom was dying from Lou Gehrig's disease.

In March, she got a letter from a producer, Helmerich and Payne, saying they owed \$25,000, which was due in ten days. \$9,000 of this amount was for the ad valorem tax, and \$16,000 for interest.

There is absolutely no way the Nicholson family has this much money available on 10 days notice. They had no advance notice whatsoever and had no prior knowledge of the entire situation. They just got a bill in the mail for \$25,000, due in 10 days. They couldn't understand how a mistake by the oil company in 1984-1985 could still apply. They contacted their attorney about the statute of limitations which would govern this situation. Even their local attorney didn't really know what to tell them. She commented to me that they certainly had not earned \$16,000 interest on the money. They had spent it. They count on their royalty checks as part of their income. In particular, it is what they used to take care of her mother.

This is the way that most of the thousands of royalty owners will be affected by FERC's actions.

By the way, Kimberly's mother passed away last month.

#### *FERC's Lack Of Jurisdiction Over Royalty Owners*

Producers have agreed that FERC lacks jurisdiction over a royalty owner. In a motion before FERC, the producers stated that:

"The Commission (FERC) purports to design around this obvious bar (Kansas House Bill No. 2419, which became K.S.A. 1998 Supp. 55-1624) by saying that the working interest owner must underwrite royalty owners' share, even though the royalty owners, not being first sellers, could not have violated the NGPA (Natural Gas Policy Act). *That is trying to do indirectly what the law denies directly: regulate the royalty owners.*

"Working interest owners cannot be the pawns in an issue of the reach of the commerce clause and the related statutes. The federal government cannot make the working interest owners take money away from non-jurisdictional royalty owners without notice and an opportunity to be heard, when to do so would violate a state statute. *It is unjust, unreasonable, and unlawful to force producers to knowingly violate of a putatively valid State law or else pay a penalty at the command of the federal government.*" (Emphasis ours)

The FERC has no jurisdiction of Kansas royalty owners and yet it has placed on Kansas producers the burden of attempting to collect the tax. The order affects thousands of Kansas royalty owners.

#### *Statute Of Limitations Arguments*

Royalty owners have also asserted that the Kansas statute of limitations bars recovery of the ad valorem tax recoupment from royalty owners. Kansas lawmakers in 1998 specifically addressed the issue and declared that the ad valorem tax refund is uncollectible due to the expiration of the statute of limitations governing such recovery and bars recovery against royalty owners. (Kansas 1998 House Bill No. 2419, which became K.S.A. 1998 Supp. 55-1624)

On May 19, 1998, in order to determine whether FERC would honor the Kansas legislation by finding that such legislation would render recovery of royalty refunds uncollectible from the royalty owners and thereby grant a waiver of those refunds, a number of producers filed a Motion in all of the pipeline dockets for a waiver of their royalty interest refunds or alternatively for a generic waiver as to all refunds attributable to royalty interests. *Public Service Company of Colorado, et al., Dockets Nos. RP97-369, et al.* This Motion attracted numerous interventions, answers, and comments, both in support and opposition. The Motion was vigorously opposed by the pipeline and gas distribution companies.

On November 2, 1998, FERC denied the motion. On the question of whether the Commission should waive the royalty owner amount of the refund obligation on a generic basis, on the basis of the statute of limitations provision of the newly enacted Kansas legislation, the Commission found that, "the recent Kansas legislation does not justify waiver of the producer's obligation to refund the royalty owner's share of the refund." The Commission stated that the purpose of Kansas House Bill 2419 appears to have been to trigger the Commission's *Wylee* (*Wylee Petroleum Corp.*, 33 F.E.R.C. (CCH) 61,014 (1985)) standard for finding the refunds attributable to the royalty owner to be uncollectible, thereby leading the Commission to waive the producer's obligation to refund those amounts to their customers.

The Order of Denial concluded that "*This order only addresses the issue of whether Kansas House Bill No. 2419 justifies waiver of ad valorem tax refunds. The Commission recognizes that there may be other Kansas statutes of limitation, such as the general contract statute of limitation in K.S.A. §60-511, which might satisfy the Wylee uncollectibility statutes of limitation in this order, since they have not been raised by the parties.*"

A request for rehearing was filed. Kansas State Senator Stephen R. Morris, R-Hugoton, who introduced the original bill (Senate Bill 685) which eventually became House Bill 2419, was very concerned by FERC's decision. In a sworn declaration before FERC on the rehearing, he stated that,

"Based on my discussions with my senate colleagues on the Ways and Means Committee, our intent in introducing SB 685 was to simplify, clarify and codify existing Kansas law, so that the public would have full knowledge that the five-year statute of limitations on bringing actions on contractual matters set forth in K.S.A. 60-511 applies to oil and gas refund matters. Thus, it would specifically apply to first sellers' attempts to collect ad valorem tax reimbursements from royalty owners, regarding ad valorem taxes paid from 1983 to 1988. SB 685 was not intended to create a new and different statute of limitations, and SB 685 does not do so.

"I also explained this need for SB 685 at a hearing held on the bill before the Senate Energy and Natural Resources Committee on March 23, 1998. Based upon my discussions with my senate colleagues on the Energy and Natural Resources Committee after receiving testimony, both written and oral, the committee also believed that the existing five-year statute of limitations in K.S.A. 60-511 prohibits first sellers from bringing an action against royalty owners for all claims that are greater than five years old. I and my colleagues were concerned that royalty owners may not be aware of the relevant statute of limitations... A conference committee report on HB 2419 was adopted by the Senate on April 2, 1998 by a vote of 38 yeas and 0 nays, and by the House of Representatives on April 8, 1998 by a vote of 120 yeas and 0 nays. The governor signed the bill on April 20, 1998.

"The purpose of simplifying, clarifying and codifying the existing five-year statute of limitations on actions in contractual matters, so that it specifically applies to first sellers' attempts to collect ad valorem tax reimbursements from royalty owners, was to prevent unnecessary litigation on such matters. Litigation by each royalty owner over claims which are barred by the statute of limitations would needlessly expend substantial resources of Kansas citizens and courts."

In spite of the clear indication of the intent of the legislation, on February 16, 1999, FERC denied rehearing on its November 2, 1998 opinion regarding the Kansas statute. FERC stated that, "nowhere in the motion (for rehearing) was there any reference to K.S.A. 60-511."

*FERC seems to have clearly ignored the spirit and intent of House Bill 2419 by declaring that when the Commission adopted the Wylee standard for uncollectibility, it did not contemplate a specifically created, ad hoc statute of limitations such as Kansas House Bill 2419, crafted to apply to a specific situation.*

It is obvious that Congressional help is needed to abate FERC's rulings.

#### *Aftermath Of FERC Decisions*

So where do things stand now? Producers are handling their royalty owners differently. A number of royalty owners have received letters from their producers or pipeline companies (or in some instances directly from FERC) demanding or requesting that they reimburse them for the Kansas ad valorem tax and interest. *However, perhaps only 5% of Kansas royalty owners have received such notices.*

SWKROA General Counsel, Gregory J. Stucky, summarized the impact of the FERC decision, as follows:

"On or about March 9, 1998, producers had to pay over money attributable to unlawful ad valorem tax payments, including sums attributable to their roy-

alty owners, to the pipeline companies or place the money into escrow if there was a dispute about the amount of money due pipeline companies from producers. Although the escrow procedures were intended only to be used when amounts actually were in controversy, many, if not most, producers, both large and small, used the escrow 'loophole' to pay virtually all the money which the pipeline companies claimed they owed into escrow, because the producers wanted to preserve every possible defense. The FERC now has before it a multitude of issues from a multitude of producers that it must deal with in connection with the escrowed money. With only a couple of staff members working on the project, it could take months, if not years, to resolve all the disputes."

"The only deadline which the producers are working against at the moment is March 9, 1999, the date that producers have to notify the FERC of any amounts that are not collectible from royalty owners. Even that date may not be considered firm by the FERC, if the producer can show some justifiable excuse for missing that date."

Taken to a more individual level, any potential refund obligation could possibly represent several years of current royalty payments, or with the compounding of interest and because of declining production could last the life of the well. Most of the money at issue is interest, which has been accruing at rates that royalty owners could not make from their own investments. Although SWKROA has membership of around 2,500, there are literally tens of thousands of royalty owners throughout the United States who are completely unaware of this potential financial bomb.

On behalf of the royalty owners I respectfully request your Sub-committee and Congress grant relief to royalty owners from the burden of this decision by FERC. What are your alternatives?

1. Seek no adjustment at all, from either producers or royalty owners, recognizing that:

- the change in FERC's decisions are unfair;
- that collection benefits only pipeline companies who at the time already had a financial edge;
- that collection efforts for a 15 year old debt will be uneven and inequitable;
- that there will be no winners, but plenty of real losers from this ruling; and
- that the statute of limitations may have expired on this issue.

2. Release producers from the burden of collecting from royalty owners, recognizing that royalty owners:

- had no control over the actions which took place;
- were already in a less-than-equitable position financially and are only being punished further; and
- FERC's ruling illegally expands their jurisdiction to regulate royalty owners.

3. At the very least, prohibit interest from being charged on royalty owners share, because it is punitive.

I started my remarks by saying that Cornell was not the typical royalty owner. Because of our resources and our involvement with SWKROA we are probably more knowledgeable and in some ways better prepared than the average royalty owner to deal with this issue. As you proceed in learning more about this issue and hopefully in becoming involved, I urge that you keep them in mind—hard working farmers and ranchers who are being punished for something they had no hand in.

Mr. BARTON. Thank you, sir.

Now we would like to hear from Mr. Albright for 5 minutes, please, sir.

#### **STATEMENT OF JAMES D. ALBRIGHT**

Mr. ALBRIGHT. Thank you, Mr. Chairman. Good morning. Good morning, members of the committee. My name is James Albright, and I am associate general counsel for New Century Services Inc. I am in-house counsel in charge of natural gas legal and regulatory matters for Public Service Company of Colorado and Cheyenne Light, Fuel, and Power Company which are natural gas distribution companies operating in Colorado and Wyoming respectively.

These two companies are pipeline customers and were principal litigants in the 1996 court case before the United States Court of Appeals for the D.C. Circuit which mandated the refunds at issue in these hearings. I am here representing the over 1 million cus-

tomers of Public Service in Cheyenne who are in line to receive \$23 million in refunds including interest resulting from the producers unlawful collection of Kansas ad valorem taxes under the Natural Gas Policy Act.

It is important to point out that the consumers, not the producers are the ones who have been aggrieved here. These consumers were overcharged on their natural gas utility bills during the 1980's as a result of the producers' unlawful collection of these taxes, and they are entitled to these refunds. Producers appropriated windfall profits during this period at the expense of gas consumers which must be returned. And because consumers have been deprived of the use of these funds for up to 16 years, they are also entitled to be kept whole through the inclusion of interest.

Now, my clients, Public Service and Cheyenne, are not unsympathetic to the small producers and royalty owners in individual cases of hardship. We have not participated in any of the cases opposing hardship except for those seeking generic relief. Many producers, however, who stand to pay these refunds are multinational oil companies with billions and billions of dollars of assets.

As the analysis submitted by Chair Lumpe in her written testimony, the top 24 producers on the list owing these refunds constitute 86 percent of the total outstanding refunds. The legal question of whether producers were entitled under the NGPA to collect this reimbursement for the Kansas ad valorem tax in their gas prices has been in dispute and the subject of litigation for over 15 years but the law itself has never changed. There has been no flip-flop.

FERC, when they made the original determination that this tax should be included as recoverable under the NGPA committed legal error, and the court so found. It misapplied the NGPA with respect to the Kansas ad valorem tax. Thus, the I.R.S. analogy is not analogous here. It was an ongoing dispute involving ongoing litigation. In the IRS analogy, that circumstance, there is two parties: the taxpayer and the government. Here there are two competing interests: the producers and the consumers.

Refunds with interest in the context of regulated industries is nothing new. The reality of Federal rate regulation which producer sales were governed by for three and a half decades is rates are collected subject to refund together with interest until a final legal determination is made. There is nothing different here. Until this litigation was finally resolved and the producers' liability for refunds confirmed and the U.S. Supreme Court denied certiorari in 1997, the producers were always in jeopardy of having to make these refunds. They should have taken account for this. These were the rules of the game.

Producers' claims of unfairness based on their detrimental reliance on prior commission orders was resoundingly rejected by the U.S. Court of Appeals for the D.C. Circuit. In the words of the court, such a claim is purely notional. And if it was real, was unreasonable and foolhardy. Considering that the matter was in dispute and the producers were on notice of the pending litigation, the court concluded, and I quote, we are hard pressed to see how the producers would be harmed in any cognizable way even if they

were required to disgorge every dollar they received in recovery of the tax.

I would like to add we are not seeking recovery of every dollar that was overcollected by these producers. The period from 1978 to 1983 is still in the producers' hands and is not at issue in these hearings. Congressional involvement simply is not warranted here. There are winners and losers in all litigation, but losers should not be entitled to run to Congress for legislative relief from the result. That is the domain of the judiciary.

Congress makes the laws and the Federal courts adjudicate disputes under those laws. Congress already established in the NGPA under section 502 the legal process for the Commission to prevent special hardship inequity or unfair distribution of burden resulting from its orders under the NGPA.

The fact of the matter is there is no sensible generic solution to address the hardship that may be experienced by producers and royalty owners from these refund obligations. Each producer's refund obligation is different. Each producer's circumstances associated with that liability are different and each producer's ability to pay the refund amounts is different. Only through consideration of the equities on an individual case-by-case basis can hardship be properly addressed.

FERC has the delegated authority under section 502 of the NGPA to address hardship claims on a case-by-case basis. Over 100 hardship cases are pending before FERC now. FERC is competent to resolve these cases equitably and expeditiously.

Last, the issue of FERC's denial of producers' petitions for generic waiver of interest on these refunds is currently pending before the U.S. Court of appeals for the D.C. Circuit. Anadarko Petroleum Company, et al. v. FERC has been fully briefed. Oral arguments are scheduled for September 7, 1999. This judicial review process was established by Congress under the NGPA pursuant to section 506.

Congress should let the judicial process run its course and allow the parties to see this litigation to its conclusion.

Mr. Chairman, before I conclude my statement, I would like to have permission to introduce the United States Court of Appeals decision on the issue in favor of the consumers be included in the record and also a resolution from the State of Nebraska and letters from nine Governors and a letter from the State of Colorado's Office of Consumer Counsel.

Mr. BARTON. Are they all relevant to the issue?

Mr. ALBRIGHT. Yes, they are, Mr. Chairman.

Mr. BARTON. Without objection so ordered.

[The information referred to follows:]

NEBRASKA UNICAMERAL LEGISLATURE  
April 28, 1999

The Honorable BOB KERREY  
United States Senate  
141 Hart Senate Office Bldg.  
Washington, DC 20510

DEAR SENATOR KERREY: I have enclosed a copy of engrossed Legislative Resolution No. 69 as adopted by the Nebraska Unicameral Legislature on the twenty-seventh day of April 1999. The members of the Nebraska Legislature have directed me

to forward this resolution to you and request that it be officially entered into the Congressional Record as a memorial to the Congress of the United States.

With kind regards,  
Sincerely,

PATRICK J. O'DONNELL  
*Clerk of the Legislature*

Enclosure

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NINETY SIXTH LEGISLATURE—FIRST SESSION

LEGISLATIVE RESOLUTION 69

*Introduced by Urban Affairs Committee: Hartnett, 45, Chairperson; Connealy, 16; Preister, 5; Smith, 48; and Bruning, 3;*

WHEREAS, until 1993, the federal Natural Gas Policy Act of 1978 established the lawful price that a natural gas producer could charge its pipeline customers for natural gas, providing under section 110 of the act that the producer could adjust the price upward in order to recover from pipeline customers any state severance tax payments made by the producer; and

WHEREAS, in 1988, in the case of *Colorado Interstate Gas Co. v. the Federal Energy Regulatory Commission*, 850 F.2d 769, the United States Court of Appeals for the District of Columbia Circuit ruled that the ad valorem tax levied by the State of Kansas was not a severance tax within the meaning of section 110 of the Natural Gas Policy Act and ordered natural gas producers to refund that portion of the payments received from the pipelines attributable to the cost of the Kansas ad valorem taxes paid plus interest; and

WHEREAS, upon remand of the matter to the Federal Energy Regulatory Commission, the commission ordered the refunds to be made on that portion of all purchases which had included Kansas ad valorem taxes which were charged after June 28, 1988, the date of the Appeals Court ruling in the *Colorado Interstate Gas Co.* case; and

WHEREAS, in 1996, in the case of *Public Service Company of Colorado v. the Federal Energy Regulatory Commission*, 91 F.3d 1478, the United States Court of Appeals for the District of Columbia overruled the commission, holding that the refunds should commence from October 1983, when notice was filed in the Federal Register of the petition before the commission challenging the propriety of including the Kansas ad valorem taxes in the price charged for natural gas produced in Kansas; and

WHEREAS, as of November 1997, the consumers of natural gas in twenty-three states were entitled, pursuant to this ruling and the subsequent order of the Federal Energy Regulatory Commission, to refunds and accrued interest from natural gas producers for the period of October 1983 through June 1988, amounting to more than \$334,840,000, with Nebraska consumers to receive approximately \$34,360,000 (approximately ten percent of the total); and

WHEREAS, of those sums, over 60 percent of the total is accrued interest as of that date with additional interest being compounded quarterly on unpaid balances and on those sums not placed in escrow accounts pursuant to commission order; and

WHEREAS, the United States Senate and the United States House of Representatives in their individual versions of the Emergency Supplemental Appropriations Act for Fiscal Year 1999 (S. 544 and H.R. 1141) have provisions, added by amendment, which would amend the Natural Gas Policy Act of 1978 to prohibit the commission or any court from ordering the payment of any interest or penalties with respect to ordered refunds of rates or charges made, demanded, or received for reimbursement of state ad valorem taxes in connection with the sale of natural gas before 1989; and

WHEREAS, both acts were adopted by their respective houses of the Congress on March 25 of this year, immediately prior to their Easter adjournment and are pending consideration by a Joint Appropriations Conference Committee; and

WHEREAS, legislation for the same purpose (S. 626 in the Senate and H.R. 1117 in the House of Representatives) is currently pending; and

WHEREAS, the sole result of the final adoption of these amendments or these bills will be to mitigate or reduce the liability of natural gas producers for charges wrongfully imposed on consumers in the period of 1983 to 1988 by denying consumers interest on the amount of those charges and relieving the producers of any liability for future penalties flowing from the failure to make court-ordered payments in the prescribed manner; and

WHEREAS, the lost refunds to Nebraska natural gas consumers will amount to more than 10 percent of the total reduction, representing the fourth largest state loss of the twenty-four states receiving court-ordered refunds; and

WHEREAS, Nebraska has been urged to join with other states in petitioning Congress to reconsider the adoption of these ill-advised and possibly unconstitutional provisions and avoid future litigation at the expense of all parties involved.

NOW, THEREFORE, BE IT RESOLVED BY THE MEMBERS OF THE NINETY-SIXTH LEGISLATURE OF NEBRASKA, FIRST SESSION:

1. That the Legislature hereby petitions the Congress of the United States to oppose the enactment of S. 626 and H.R. 1117 or any version thereof which would have the effect of waiving \* \* \*

STATE OF COLORADO  
OFFICE OF CONSUMER COUNSEL  
DEPARTMENT OF REGULATORY AGENCIES  
June 4, 1999

The Honorable JOE BARTON, *Chairman*  
The Honorable RALPH M. HALL  
*Subcommittee on Energy and Power*  
*House of Representatives*  
*Commerce Committee*  
*2125 Rayburn House Office Building*  
*Washington, DC 20515-6115*

RE: Kansas *ad valorem* Tax Refund

GENTLEMEN: As Director of the Colorado Office of Consumer Counsel I would like to express my concerns regarding H.R. 1117. My office represents approximately 1,500,000 residential, agricultural and small business gas consumers in the state of Colorado that have been illegally charged Kansas *ad valorem* taxes in their gas rates. H.R. 1117 would deny Colorado consumers almost \$20 million in interest out of a \$30 million refund that would otherwise be due to these consumers.

Colorado's low-income consumers in particular will be adversely affected if the bill passes. Colorado law requires that up to 90 percent of any unclaimed refunds be paid to the Colorado Energy Assistance Foundation to help low-income consumers pay their utility bills. Because the refund dates back to 1983-1988, the unclaimed portion of the refund will be substantial. If Congress eliminates the interest and reduces the amount of the refund, the foundation will have less to distribute to low-income consumers.

I recognize that some gas producers claim the interest obligation is a hardship. However, the large gas producers have been on notice about this refund since 1983. They made no attempt to provide for the eventual refund of these amounts. Instead they fought the refund at every turn. Small consumers have been waiting for years to have their money returned while producers are exhausting all possible means to keep the illegally collected amounts. That is a real hardship for small consumers. In any event, the refund procedures of the Federal Energy Regulatory Commission take into account the hardship claims and there is no need for Congressional intervention.

The Office of Consumer Counsel urges you to ensure that Colorado consumers receive the refunds to which they are entitled.

Very truly yours,

KEN REIF  
*Director*

cc: Honorable Thomas J. Bliley Jr., Chairman, Commerce Committee  
Honorable John D. Dingell  
Honorable Diana DeGette

May 10, 1999

Chairman C.W. "BILL" YOUNG  
*House Appropriations Committee*  
*H-218, United States Capitol*  
*Washington, D.C. 20515*

DEAR CHAIRMAN YOUNG: We would like to ask for your assistance in deleting Amendment 101 that was included in the Senate Emergency Supplemental Appropriations Bill (S. 544) by Senator Pat Roberts (R-KS). This amendment would waive approximately \$235 million of accrued interest on refunds of Kansas *ad valorem*

taxes. The amendment would have a detrimental effect on natural gas consumers from 23 states, and we urge you to oppose its inclusion in the conference report.

Between 1983 and 1988, Kansas natural gas producers collected *ad valorem* taxes on natural gas that was purchased by numerous interstate pipelines in Kansas and transported elsewhere. In 1997, the Federal Energy Regulatory Commission (FERC) ordered refunds of these taxes based on a final decision of the D.C. Circuit Court of Appeals. The issues of whether interest should be paid on refunds of the taxes collected prior to 1989 is currently before the D.C. Circuit with oral argument scheduled for September 7, 1999. Consequently, we believe that it would be improper for Congress to intervene at this time.

Consumers in 23 states, including our states, are entitled to refunds and to the interest on those refunds. Of the estimated \$363 million of total refunds owed as of March 31, 1999, more than \$235 million of this was accrued interest and would be lost.

Please oppose the inclusion of the Roberts amendment, which would prohibit payment of interest on the refunds that are due. On behalf of natural gas consumers across the country, thank you for your assistance in eliminating this amendment from the conference report.

Sincerely,

GOVERNOR VENTURA OF MINNESOTA  
GOVERNOR VILSACK OF IOWA  
GOVERNOR CARNAHAN OF MISSOURI  
GOVERNOR HULL OF ARIZONA  
GOVERNOR O'BANNON OF INDIANA  
GOVERNOR JOHANNNS OF NEBRASKA  
GOVERNOR JANKLOW OF SOUTH DAKOTA

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*2462 Rayburn House Office Building*  
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May 12, 1999

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*H-218, United States Capitol*  
*Washington, D.C. 20515*

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TOMMY G. THOMPSON  
*Governor of Wisconsin*

May 12, 1999

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May 11, 1999

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*Washington, D.C. 20515*

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M.J. FOSTER  
*Governor of Louisiana*

May 12, 1999

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*House Appropriations Committee*  
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*Governor of Louisiana*

Mr. BARTON. Does that conclude your statement?

Mr. ALBRIGHT. That concludes my statement, Mr. Chairman. Thank you.

[The prepared statement of James D. Albright follows:]

PREPARED STATEMENT OF JAMES D. ALBRIGHT, ASSOCIATE GENERAL COUNSEL, NEW CENTURY SERVICES, INC.

#### INTRODUCTION

Mr. Chairman and members of the committee, my name is James D. Albright. I am Associate General Counsel, New Century Services, Inc., a wholly-owned subsidiary of New Century Energies, Inc. My responsibilities in that capacity include all regulatory and legal matters regarding natural gas for Public Service Company of Colorado (Public Service) and Cheyenne Light, Fuel and Power Company (Cheyenne), both wholly-owned subsidiaries of New Century Energies, Inc. Public Service and Cheyenne are combination electric and gas utilities. As relevant to these hearings, Public Service and Cheyenne are local distribution companies that provide retail natural gas service to customers that is extensively regulated by their respective state utility commissions. Both Public Service and Cheyenne purchased natural gas during the 1980's from interstate pipelines which, in turn, purchased natural gas produced in various states, including the State of Kansas. Public Service and Cheyenne together serve over one million natural gas customers in Colorado and Wyoming. Public Service and Cheyenne were the lead petitioners in the 1996 federal court case mandating the refunds which are the subject of these hearings. Although Public Service and Cheyenne do not stand to retain any of these refunds—as, pursuant to applicable state regulatory requirements, virtually all of the refunds will be passed through to customers—Public Service and Cheyenne have found themselves championing the interests of natural gas consumers in the 23 states who would receive these refunds.

The purpose of these hearings, as I understand it, is to consider whether Congress should entertain legislation that would forgive interest on refunds ordered by the Federal Energy Regulatory Commission (FERC) to be paid by first sellers, primarily natural gas producers, who sold natural gas from 1983 to 1988 at prices which exceeded the maximum lawful prices prescribed under the Natural Gas Policy Act of 1978 (NGPA). These over collections are attributable to the producers including, as an add-on to the gas prices charged, reimbursement for *ad valorem* taxes paid to the State of Kansas which were ultimately found by the FERC, and affirmed by the United States Court of Appeals for the District of Columbia Circuit in *Public Service Co. of Colorado, et al. v. FERC*, 91 F.3d 1478 (D.C. Cir. 1996), cert. denied 520 U.S. 1224 (1997), to be ineligible as an add-on under section 110 of the NGPA.

I am pleased to appear here today to explain how the producers' refund obligation came about and why it would be inappropriate for Congress to excuse the interest component of these refunds. First and foremost, the committee should not forsake the gas consumers who were illegally overcharged in their natural gas bills as a result of these over collections. These consumers have been waiting a long time for these refunds. Interest on these refunds merely puts these consumers in the position they would have been in had the illegal overcharges not occurred. Fairness and equity is on the side of the consuming public, not on the side of the gas producing enterprises that exacted excess revenues through illegal gas prices. In addition, I urge the committee not to undercut our right to complete the legal process established by Congress in the NGPA for the very purpose of resolving disputes such as this.

At the outset I would like to point out that the vast majority of the monies to be refunded will not come from "Kansas" producers—if that term is intended to imply that the producers owing the refunds are Kansas corporations or other persons living in Kansas. Rather, the vast majority of the dollars to be refunded will come from "major" producers which are not Kansas corporations, such as Amoco Production Company, Anadarko Petroleum Corporation, Union Pacific Resources Corporation, Mobil Oil Corporation, and OXY USA Inc. These major international oil companies are also not "small" producers. For example, Amoco has a market capitalization of \$174.5 billion, Anadarko has a market capitalization of \$4.6 billion, and Union Pacific Resources has a market capitalization of \$3.59 billion.

I would also like to point out, as I am sure the committee is aware, that there is currently pending in the D.C. Circuit, in *Anadarko Petroleum Corporation, et al. v. FERC*, Nos. 98-1227, *et al.*, a judicial review proceeding brought by these large producers under section 506 of the NGPA in which they challenge the legality of FERC's decision to deny a generic waiver of interest on the refunds mandated by *Public Service Co. of Colorado*. The exact same relief sought by the producers, which

was denied by the FERC and is pending before the D.C. Circuit, is now presented to this committee for its consideration in these hearings.

NGPA section 506(4) provides that “[t]he judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final subject to review by the Supreme Court of the United States upon certiorari...” This is the process established by Congress in the NGPA for resolving disputes over the rights and obligations of the parties under the statute and the rules by which the parties have been bound for over 20 years. I urge this committee not to disrupt the ongoing judicial process and deprive us of the procedural rights established by the NGPA simply because the total interest on the refunds is substantial and there may be individual cases of hardship. The interest is substantial because the producers have held and used money that was not theirs for a period in the range of 11 to 16 years. Moreover, the procedure provided for in the NGPA provides FERC with jurisdiction under section 502(c) to weigh the equities in individual cases of hardship and determine whether or not adjustment relief is required. The procedures for NGPA section 502(c) adjustments have been in place and used for over 20 years. Requests for adjustments related to the Kansas *ad valorem* tax, recently filed with the FERC, number over one hundred. The resolution of these cases is proceeding under the FERC’s duly-promulgated regulations and that process should not be short-circuited by the Congress.

It should be clear that there is no inequity or injustice in requiring producers to pay interest on amounts in excess of the roughly \$100 million they overcharged their customers from 1983 to 1988. There is also no inequity or injustice in requiring producers to demonstrate the kind of *individualized* showing of hardship required by NGPA section 502(c) if FERC is to grant an exception. Under our American system of justice, there is a general obligation to compensate judgment creditors through the payment of interest on the principal amount of outstanding liabilities. The payment of interest here is necessary to make whole the gas customers who were overcharged and denied the use of their money for up to 16 years. Were Congress to forgive the interest overcharged customers it would be allowing producers to retain the earnings on consumer dollars and would strip the consumers, by legislative action, of over \$200 million (more than 60%) of their claim.

Not only would there be unfairness and inequity in failing to make consumers whole for these illegal overcharges, a legislative forgiveness of interest would unduly discriminate in favor of natural gas produced in Kansas and the state treasury of Kansas over natural gas produced in other states and their state treasuries. Other gas producing states, including particularly Texas, also have *ad valorem* or other property-type taxes which have never been eligible for reimbursement as an add-on to the maximum lawful price under the NGPA. Texas’s *ad valorem* tax, which in all material respects was identical to Kansas’s *ad valorem* tax, was expressly found by the FERC in 1986 not to qualify as a recoverable “add-on” to the maximum lawful price under section 110 of the NGPA. Thus, gas producers in Texas and other gas producing states have never been allowed to collect reimbursement for these types of state taxes in the prices charged for natural gas. To forgive interest on these refunds would prefer producers of Kansas gas over producers of gas from other states.

As is apparent from the history of the producers’ obligation to refund the excessive collections, which this committee requested I address, the producers’ claim that they relied to their detriment on FERC’s rulings that they could legally collect the Kansas tax under the NGPA lacks credulity. The bankruptcy of that plea was recognized by the D.C. Circuit which, in *Public Service Co. of Colorado v. FERC*, referred to the producers’ detrimental reliance claim as “purely notional,” adding that, “if real,” it was both “unreasonable” and “foolhardy.” 91 F.3d at 1490.

#### HISTORY BEHIND THE REFUND OBLIGATIONS

On November 9, 1978, the NGPA became law. In an effort to encourage production in the aftermath of natural gas shortages experienced during the 1970’s, Congress removed producer pricing from the strictures of cost-based price regulation under the Natural Gas Act (NGA) and established uniform, incentive ceiling prices for various categories of natural gas production. As a part of the statutory scheme, Congress made those new prices ceiling prices which could not be exceeded except to the extent specifically allowed under NGPA section 110. NGPA section 110 provided, among other things, for an “add-on” to the maximum lawful price for “State severance taxes”—a term defined in section 110(c) of the NGPA. The NGPA further declared that sales of gas at prices which exceeded the ceiling prices were “unlawful.” FERC was charged with administration of the NGPA with full authority to issue such orders as it deemed necessary and appropriate to carry out its functions

under the statute. See NGPA Section 501. The statutory scheme enacted by Congress in the NGPA was well recognized as one which substantially overhauled federal regulation of natural gas prices.

While under NGA price regulation, the Federal Power Commission (FERC's predecessor agency) had allowed the cost of Kansas *ad valorem* taxes to be added to the then-applicable cost-based national ceiling price of gas. *Just and Reasonable National Rates for Sales of Natural Gas*, Opinion No. 699-D, 52 FPC 915 (1974). The FPC had also determined that the cost of Texas *ad valorem* taxes could not be added to the then-applicable cost-based national ceiling price of gas. *Mobil Oil Corp.*, 55 FPC 917 (1976). Possibly because of the regulatory upheaval caused by the NGPA and the need for FERC to promulgate comprehensive regulations to implement the new statutory scheme, it was not until 1983 that the continued validity of the FPC's prior treatment of these two *ad valorem* taxes under the NGA was challenged under the NGPA.

In January 1983, Sun Exploration and Production Company, a producer and first-seller of gas, filed a petition at the FERC seeking a determination that the Texas *ad valorem* tax was a "State severance tax" as defined in NGPA section 110(c) and, therefore, could be collected as an add-on to the maximum lawful price. Shortly after this petition was filed, Northern Natural Gas Company, a pipeline purchaser of gas, filed a petition at the FERC seeking a similar determination that the Kansas *ad valorem* tax was not a "State severance tax" as defined in NGPA section 110(c) and, therefore, could not be collected as an add-on to the maximum lawful price.

FERC consolidated the petitions and, in a decision issued in 1986, denied both. It ruled that the Texas *ad valorem* tax was a property tax, not a State severance tax and, therefore, the ceiling price of gas produced in Texas could not include an amount to reimburse the producer for the Texas *ad valorem* tax. FERC also ruled that the Kansas *ad valorem* tax was a State severance tax and, therefore, the ceiling price of gas produced in Kansas, unlike the ceiling price of gas produced in Texas, could include an amount to reimburse the producer for the Kansas *ad valorem* tax. *Sun Exploration and Production Co.*, 36 FERC ¶61,093 (1986).

Sun Exploration did not seek rehearing of the order. However, Northern Natural Gas Company and Colorado Interstate Gas Company, pursuant to NGPA section 506, filed petitions for rehearing of the FERC's ruling regarding the qualification of the Kansas *ad valorem* tax as a "State severance tax" under the NGPA. When the petitions were denied in *Northern Natural Gas Co.*, 38 FERC ¶61,062 (1987), Colorado Interstate Gas Company filed a petition for review in the United States Court of Appeals for the District of Columbia Circuit, following the procedure mandated by NGPA section 506.

After reviewing the Commission's order classifying the Texas tax as a "property" tax and the Kansas tax as a "severance" tax, the D.C. Circuit, in *Colorado Interstate Gas Co. v. FERC*, 850 F.2d 769 (D.C. Cir. 1988), found that the dissimilar treatment of what seemed to the Court to be identical cases was the "quintessence of arbitrariness and caprice." 850 F.2d at 774. The Court remanded the case back to the FERC for the FERC "to exercise its interpretive authority, to identify the features of the Kansas tax that point toward one classification or another, and to offer sensible distinctions between taxes that it chooses to treat differently." 850 F.2d at 774-775.

On remand, the FERC re-examined the Kansas tax under the statutory standard of NGPA section 110(c) and determined that the Kansas tax, after all, did not qualify as a tax "imposed on the production of natural gas"—the statutory requisite for a "State severance tax"—because, like the Texas tax, the Kansas tax was a tax on "property," not a tax on production. As such, like the Texas tax, the Kansas tax was not eligible as an add-on to the otherwise applicable NGPA maximum lawful price. *Colorado Interstate Gas Co.*, 65 FERC ¶61,292 (1993). Having so ruled, FERC recognized that "reimbursement of that tax in addition to the ceiling [price] violates the Congressionally-set maximum lawful prices." 65 FERC ¶61,292. Nevertheless, responding to the producers' claims that they had relied to their detriment on the Commission's prior rulings, the Commission decided that the producers had certain "settled expectations" to the collection of the unlawful amounts and, therefore, required refunds only from June 28, 1988—the date of the D.C. Circuit's remand order.

Petitions for rehearing were filed by the producers challenging the Commission's decision that the Kansas tax was a "property" tax, and by Public Service and Cheyenne challenging the Commission's decision to waive refunds for the 1983 to 1988 period. The Commission denied all of the rehearing petitions in *Colorado Interstate Gas Co.*, 67 FERC ¶61,209 (1994).

Again, following the procedures established in NGPA section 506, petitions for review were filed by the producers and jointly by Public Service and Cheyenne. In the judicial review proceeding, the producers argued that it would be unfair to require

producers to refund any of the pre-1988 over collections because, until the FERC issued its 1993 decision in *Colorado Interstate Gas Co.*, the producers had no reason to believe that any refunds would be owed. Public Service and Cheyenne argued that the FERC should not have waived refunds for the pre-1988 period because the legitimacy of the collection of the Kansas *ad valorem* tax under the NGPA had been disputed in ongoing litigation since 1983 and, consequently, there could not have been any "settled expectation" to the retention of the overcharges on which the producers could have relied to their detriment. In *Public Service Co. of Colorado, et al. v. FERC*, 91 F.3d 1478 (D.C. Cir. 1996), the D.C. Circuit affirmed the Commission's determination that the Kansas tax was a "property" tax and not a tax on production that was eligible for reimbursement under the NGPA. The court also rejected outright the producers' "detrimental reliance" argument. The court concluded that *all* of the producers' collections of reimbursements for the Kansas tax that were in excess of the maximum lawful NGPA price had been unlawful since 1978 and should be refunded *but for* the simple fact that the issue of pre-1983 refunds was not before the Court. The Court, therefore, concluded that refunds for the period 1983 to 1988 were required. The following excerpt from the D.C. Circuit's decision says it best:

Not only is the producers' "detrimental reliance" purely notional; if it were real it would not have been reasonable. The enactment of a substantially new regulatory regime in 1978 undermined any assurance that the FPC's treatment of the Kansas tax under the NGA would withstand scrutiny under the NGPA; reliance would have been foolhardy. If that were not enough, the status of the Kansas tax was expressly drawn into question in 1983 when Northern Natural first petitioned the Commission for a ruling that producers could not lawfully recover the tax under § 110. Once the recoverability of the tax was in dispute, we do not see how the Commission could possibly find that producers reasonably relied upon continuing to recover it.

Because no seller of natural gas could justifiably be confident that it was entitled to recover the tax until the legal question was settled anew under the new statute, we hold that the producers' liability for refunds extends back to October 1983, the date when all interested parties were given notice in the Federal Register that the recoverability of the Kansas tax under § 110 of the NGPA was at issue, and the earliest date advocated by any party before this court. Absent detrimental and reasonable reliance, anything short of full retroactivity (*i.e.*, to 1978) allows the producers to keep some unlawful overcharges without any justification at all. The court strongly resists the Commission's implication that the Congress intended to grant the agency the discretion to allow so capricious a thing. Still, we do not require refunds of taxes recovered with respect to production before October 1983 because there is before us no controversy over those monies.

91 F.3d at 1490.

The producers attempted to obtain review of the D.C. Circuit's decision in the United States Supreme Court but, following the advice of the Solicitor General of the United States, the Supreme Court denied their petition for certiorari.

The legal review of the issue having been concluded, it was left to the FERC to implement the Court's mandate. Immediately following the Supreme Court's ruling denying their petition for certiorari, the producers filed a request with the FERC for generic adjustment under NGPA section 502(c) asking for a blanket, all inclusive waiver of the obligation to pay interest on the overcharges. Their argument before FERC was the same as it had been before the Court; *i.e.*, relief from the interest component of the refunds was required because they had relied to their detriment on prior agency orders. Four days later, Public Service and Cheyenne filed a joint petition requesting the Commission to establish procedures for the refund of the 1983 to 1988 over collections with interest. Public Service's petition urged the Commission to follow virtually the same procedures that it had adopted in 1993 in ordering refunds of the 1988 to 1993 over collections, which have since been refunded. The Commission denied the producers' request and granted the joint petition of Public Service and Cheyenne. In so ruling, the Commission rejected the producers' request for a generic waiver of the interest component of refunds, concluding that it could not see "how the same reliance that in the context of waiving all refunds for the 1983-1988 period the Court concluded was foolhardy, can somehow be transformed into reliance that would justify granting adjustment relief of interest." *Public Service Co. of Colorado*, 80 FERC ¶61,264 at 61,216 (1997). Petitions for rehearing were filed by the producers and, when those petitions were denied, the review petition in *Anadarko Petroleum Corp., et al. v. FERC, Nos. 98-1227, et al.* was filed. As I explained earlier, this case is now pending before the D.C. Circuit. Briefing is completed and oral argument is scheduled for September 7, 1999.

Reviewing this history and the arguments advanced by the producers, it is clear that they have brought their plea to Congress because they have lost before the court and the Commission and fear losing again. Again, they press the claim that they relied to their detriment on prior agency orders, but this time they make the claim before Congress, asking Congress to undermine the very process it enacted and has had in place for over 20 years for resolving these sorts of claims. The Court of Appeals for the D.C. Circuit fully considered their argument and rejected it—calling their claim to be “purely notional” or, “if real,” “foolhardy” and “unreasonable.” Congress should not intervene on behalf of the losing party in court litigation and alter the outcome of the very judicial process it put in place—especially here, where the issue involves the return of unlawfully collected overcharges for the sale of natural gas.

The real problem with the producers’ “reliance” argument is that it is not believable. It does not pass the “red face” test. The producers themselves initiated action before the FERC questioning the continued validity of the FPC’s NGA ruling regarding the Texas tax. From that point forward, the issues regarding the Texas tax and the Kansas tax were joined. At all times relevant here (1983-1988), while the producers were collecting from their customers reimbursements for the Kansas *ad valorem* tax in addition to the maximum lawful price, the qualification of the tax as a “State severance tax” under the NGPA was disputed and the subject of litigation—the result of which would either be that the tax qualified and no refunds were due or that it did not qualify and refunds would have to be made. And that is as true for the interest component of the refunds as it is for the principal component. FERC’s regulations throughout this period specifically provided that all prices collected for the first sale of natural gas were collected subject to a general obligation to refund any portion “together with interest” that exceeded the applicable maximum lawful price established by Congress. 18 C.F.R. § 270.101(e).

#### CONCLUSION

As an active party to the proceedings before the FERC and as the primary advocate in the Court of Appeals for the refund of these over collections, with interest, to those who were overcharged, we urge the committee to consider whether it is appropriate for Congress to usurp the judicial power and truncate the rights of litigants already before the courts. Congressional intervention is simply not warranted. The status of this matter is that, after 16 years, the customers’ rights to the return of unlawfully collected and unlawfully held amounts (over \$300,000,000) has finally been determined subject only to review by the United States Court of Appeals. This is the process Congress established when it enacted section 506 of the NGPA. Congress should not step in now to cut that process short and reverse the outcome before the Court of Appeals can consider the case before it. To do so would be no different than if Congress passed a law allowing banks to charge only “service fees,” defined by statute, and class action litigation ensued for many years over whether banks had unlawfully charged their customers \$100 million that did not qualify as a “service fee” under the statute. Finally, just after the customers prevail and are awarded their \$100 million plus interest by the courts, the United States Congress passes a law excusing the banks from paying interest simply because the banks *thought* their fee qualified as a “service fee” and did not expect to lose the litigation. Clearly, the customers would not be made whole if Congress were to take such action. It is no different here.

In this case, the producers’ obligation to refund the overcharges was determined finally in May 1997, when the Supreme Court denied the producers’ petition for certiorari. It is now June 1999. For the last two years, despite the fact that the obligation to pay at least the principal amount has been clear, only one large producer, Mobil Oil Corporation, has paid the refunds it owes. The others, including Anadarko Petroleum Corporation, Amoco Production Company, Union Pacific Resources Corporation, and OXY USA Inc. have refused to refund one dollar. Instead, they are allowing interest to continue to accrue by their own refusal to refund even the principal amounts.

We ask the committee not to interfere with the judicial process and the adjudication of our rights under the NGPA. We urge you not to change the rules in the bottom of the 9th inning. The decision of the D.C. Circuit in *Anadarko Petroleum Corp., et al. v. FERC* should be the *final* determination of the rights of the parties to interest on the principal amount of the overcharges, subject only to review by the Supreme Court of the United States, as specified in section 506 of the NGPA.

This concludes my written statement.

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## United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

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Argued January 12, 1996

Decided August 2, 1996

No. 94-1418

PUBLIC SERVICE COMPANY OF COLORADO, ET AL.,  
PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION,  
RESPONDENT

OXY USA INC., ET AL.,  
INTERVENORS

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Consolidated with  
94-1481, 94-1489, 95-1138

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On Petitions for Review of an Order of the  
Federal Energy Regulatory Commission

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*Mark L. Evans* argued the cause for petitioner Anadarko Petroleum Corporation, et al. (Producer Petitioners), with

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Bills of costs must be filed within 14 days after entry of judgment. The court looks with disfavor upon motions to file bills of costs out of time.



whom *John S. Martin* was on the briefs. *Thomas R. Schwarz, Jr.* argued the cause for petitioner Missouri Public Service Commission, with whom *David W. D'Alessandro* and *Kelly A. Daly* were on the briefs. *Karol L. Newman* argued the cause for petitioners Public Service Company of Colorado and Cheyenne Light, Fuel and Power Company, with whom *James D. Albright* was on the briefs.

*Eric L. Christensen*, Attorney, Federal Energy Regulatory Commission, argued the cause for respondent, with whom *Jerome M. Feit*, Solicitor, was on the brief.

*Thomas R. Schwarz, Jr.* and *David W. D'Alessandro* were on the brief for intervenor Missouri Public Service Commission. *Penny G. Baker* entered an appearance. *Emery J. Biro, III, Jay G. Martin, Douglas F. John, Kevin M. Sweeney, Kerry R. Brittain* and *Norma J. Rosner* were on the brief for intervenors in support of respondent. *Mark L. Evans, Jay G. Martin, Marge O'Connor, J. Stephen Martin* and *Kerry R. Brittain* were on the brief for the Producer Intervenors. *Gary W. Boyle* was on the brief for intervenor Williams Natural Gas Company. *Martin J. Bregman* entered an appearance for intervenor Western Resources, Inc. *Donald C. Shepler, Jr.* and *James Howard* entered appearances for intervenor Colorado Interstate Gas Company. *Bruce A. Connell* entered an appearance for intervenor Conoco, Inc. *Michael L. Pate* entered an appearance for intervenor OXY USA, Inc. *Frank X. Kelly, George J. Meiburger, Mark C. Schroeder* and *Steve Stojic* entered appearances for intervenor Northern Natural Gas Company. *Kathy L. Cox* entered an appearance for intervenor Union Pacific Resources Company. *Andra B. Greene* and *Buddy J. Becker* entered appearances for intervenor K N Energy, Inc. *Thomas R. O'Donnell* entered an appearance for intervenor Public Service Company of Colorado and Cheyenne Light, Fuel and Power Company. *Andrew N. Greene* and *Elisabeth Y. Pendley* entered appearances for intervenor K N Interstate Gas Transmission Co. *James F. Moriarty* entered an appearance for intervenor Missouri Gas Energy.

Before: WILLIAMS, GINSBURG and SENTELLE, *Circuit Judges*.

Opinion for the Court filed by *Circuit Judge* GINSBURG.

Concurring Opinion filed by *Circuit Judge* SENTELLE.

GINSBURG, *Circuit Judge*: Until 1993 the Natural Gas Policy Act (NGPA) established the maximum lawful price that a producer could charge its pipeline customers for natural gas; under § 110 of the Act, the producer could adjust that price upward in order to recover its payment of a state severance tax. The Federal Energy Regulatory Commission, on remand from our decision in *Colorado Interstate Gas Co. v. FERC*, 850 F.2d 769 (1988), held that *ad valorem* taxes levied by Wyoming and Colorado are, but the *ad valorem* tax levied by Kansas is not, a severance tax within the meaning of § 110. The Commission then ordered producers to refund payments received from pipelines in recovery of the Kansas tax with respect to production occurring after the *Colorado Interstate* decision. The Commission directed the pipelines in turn to channel those refunds to their customers, but decided not to make the pipelines liable for any amounts not received from producers.

Petitioner Public Service Company of Colorado and a subsidiary (jointly PSCC), supported by the Missouri Public Service Commission (MPSC) as an intervenor, challenge the Commission's authority to limit the retroactivity of the producers' liability for refunds of the Kansas tax. As a petitioner the MPSC also objects to the Commission's order relieving Williams Natural Gas Company of any obligation to guarantee the refund of the Kansas taxes that Williams collected from its customers, as to which Williams intervenes in support of the FERC, and to the Commission's decision that the Wyoming and Colorado taxes are severance taxes.

Four producers petition for review of the Commission's decision that the Kansas tax is not a severance tax. These Producer Petitioners also maintain that the FERC's decision worked a change in the law that should be applied prospectively only. As Producer Intervenors the same group argues in the alternative that the Commission properly limited their

liability for the refunds of the Kansas tax to the date of the *Colorado Interstate* decision. Joined by another producer, the five so-called Indicated Producers intervene in support of the Commission regarding the Wyoming and Colorado taxes.

We conclude that the Commission could properly determine that the Kansas *ad valorem* tax was, and that the Colorado and Wyoming *ad valorem* taxes were not, sufficiently similar to a severance or production tax to qualify for recovery under § 110 of the NGPA. Contrary to the Commission, however, we hold that the producers must refund all the Kansas taxes they collected since October 1983 when all interested parties were first put on notice that the taxes might not be recoverable under § 110. On the question whether Williams should be required to guarantee the refunds due from its producers to its customers, we find no ground upon which to require that the FERC hold the pipeline liable.

### I. Background

From 1978 until 1993 producer prices for natural gas were subject to maximum lawful levels specified in the NGPA. 15 U.S.C. §§ 3311-19. Section 110 of the NGPA permitted a producer to charge an amount in excess of those ceilings to the extent necessary to recover its payment of "State severance taxes attributable to the production of such natural gas," 15 U.S.C. § 3320(a)(1). For this purpose, a severance tax was defined as "any severance, production, or similar tax, fee, or other levy imposed on the production of natural gas" by a state or Indian tribe, 15 U.S.C. § 3320(c).

In *Sun Exploration and Production Co.*, 36 FERC ¶ 61,093 (1986), the Commission determined that the Kansas *ad valorem* tax qualified as a severance tax under § 110 because it was based upon production factors. In *Colorado Interstate* we concluded that the Commission's analysis in *Sun Exploration* "fell short of reasoned decision-making," and we remanded the matter for a more "cogent theory of what makes a tax 'similar' to a production or severance tax under § 110." 850 F.2d at 770, 773. Reflecting our indulgent standard of review for a question so bound up in administrative policy-making,

we noted that while the court “cannot defer to a vacuum,” we would defer to “any Commission interpretation of § 110 that is not precluded by the statutory language and traditional methods of statutory construction, and that is reasonable.” *Id.* at 774.

We also offered the Commission some guidance. A severance tax is a cost imposed upon producing, while a property tax is a cost imposed upon holding, a resource; the non-recoverability of a severance tax is a disincentive to produce, while the non-recovery of a property tax is not a disincentive and, to the extent that extraction reduces the value of the reserves to which the property tax is applied, might even be an incentive to produce. *Id.* at 771. On the other hand, if in computing the value of a property for the purpose of levying a property tax “a state sought to capitalize the annual production (or revenue) enjoyed by each producer by multiplying it by a single fixed figure, the [property] tax would plainly be similar enough to a production tax to qualify under § 110.” *Id.* at 772.

Upon remand, the Commission identified two essential differences between a severance tax and a property tax:

First, a . . . severance tax is *on* the volume or value of the commodity *removed*, as assessed at the time of removal. A property tax . . . is on the value of the gas remaining in the ground as well as on the value of wells and other production assets on the lease, at the time of the tax assessment.

Second, . . . once the unit of gas is produced and the severance tax is applied to it, that unit of gas is never again subject to the severance tax. On the other hand, a property tax . . . is applied to a unit of gas reserves each year—year after year—until that unit of gas finally is produced and removed from the property being valued.

*Colorado Interstate Gas Co.*, 65 FERC ¶ 61,292 at 62,370–71 (1993) (emphases in original) (hereinafter *Colorado Interstate Remand Order*), *reh’g denied*, 67 FERC ¶ 61,209 (1994) (hereinafter *Colorado Interstate Rehearing Order*). Applying

these distinctions, the Commission concluded that the Kansas tax did not qualify as a severance tax for three principal reasons: (1) it was based upon the value of the gas property rather than upon its current production; (2) the volume of production was relevant principally for determining the present value of the gas reserves; and (3) the reserves were taxed year after year until removed from the ground and sold. *Id.* at 62,371-72.

The Commission ordered producers to refund the Kansas taxes they had collected since June 1988, the date of our *Colorado Interstate* decision which, in the FERC's view, first put producers on notice that the tax might not be recoverable under § 110. *Id.* at 62,373. The Commission also ordered pipelines to flow-through the refunds to customers as lump sum payments, but the pipelines were not held responsible for guaranteeing payment if a producer failed to meet its refund obligation. *Id.* at 62,374.

Williams, one of the pipelines ordered to refund the Kansas tax, had also collected Wyoming and Colorado *ad valorem* taxes from its customers. In *Williams Natural Gas Co.*, 69 FERC ¶ 61,373 (hereinafter *Williams Order*), *reh'g denied*, 70 FERC ¶ 61,202 (1994) (hereinafter *Williams Rehearing Order*), the Commission held that the Wyoming and Colorado taxes qualified as severance taxes under § 110. The Wyoming tax "is assessed on the volume or value of the gas which is produced" and "varies directly, and exclusively, with actual production." *Id.* at 62,408. The Colorado tax is "assessed only against gas that is severed from the ground." *Id.* at 62,410. Therefore, Williams was not required to refund these taxes to its customers.

## II. Analysis

We turn first to the question whether the Commission was reasonable in holding that the Kansas tax was recoverable under § 110. Next we undertake a similar inquiry with respect to the Colorado and Wyoming taxes. Then we examine the date to which refund liability for the Kansas tax extends; and finally we review the FERC's decision not to

hold Williams responsible as a guarantor in the event that a producer does not meet its refund obligation.

#### A. *The Kansas Tax*

Our review of the Commission's interpretation of § 110 of the NGPA is governed by the familiar analysis of *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984): if the Congress has "directly spoken to the precise question at issue," the court "must give effect to the unambiguously expressed intent of Congress"; otherwise the court will defer to the administering agency's interpretation if it is reasonable in light of the structure and purpose of the statute. *Id.* at 842-43. In this instance, recall that § 110 of the NGPA permits a producer to "recover . . . State severance taxes attributable to the production of . . . natural gas and borne by the seller," 15 U.S.C. § 3320(a)(1), and that a severance tax is defined as "any severance, production, or similar tax, fee, or other levy imposed on the production of natural gas." 15 U.S.C. § 3320(c). In their application to a particular state tax, any or all of the terms "attributable to the production," "similar," "other levy," and "imposed on the production" may be ambiguous. Plainly, as the Producer Petitioners acknowledge, our standard of review is that of *Chevron* step two.

The Kansas tax is levied primarily upon the value of recoverable reserves and secondarily upon the value of gas well equipment and materials. In estimating the volume of reserves, the volume of current production is an important factor; therefore, because the tax is partly dependent upon production, the Producer Petitioners allege that it is similar to a production tax.

In remanding *Colorado Interstate* we instructed the Commission to come up with a "cogent theory of what makes a tax 'similar' to a production or severance tax under § 110." 850 F.2d at 773. The agency's determination was to hinge upon "how the specific rules of the tax actually function." *Id.* at 774. According to the Producer Petitioners, however, the Commission responded largely by ignoring the practical ap-

plication of the Kansas tax and its actual effect upon production incentives, and focused instead upon mere labels.

The principle advanced by the Producer Petitioners is that “a tax whose assessment is measurably affected by a change in the level of production is at least in part attributable to, and effectively imposed on, the production itself.” The Petitioners remind us that the Federal Power Commission held that the Kansas tax was recoverable under the Natural Gas Act, Opinion No. 699-D, 52 FPC 915, 915-16 (1974), and that the Congress incorporated into § 110 of the NGPA terms virtually identical to those it had used in the prior statute, *see* Opinion No. 699, 51 FPC 2212, 2301, *reh'g denied in relevant part*, 52 FPC 1604 (1974), *aff'd sub nom. Shell Oil Co. v. FPC*, 520 F.2d 1061 (5th Cir. 1975)—which suggests that the Congress intended no significant contraction in the range of severance taxes that could be recovered. Indeed, the Conference Committee Report on § 110 states that the term “severance tax” should be “construed broadly” and may extend to “any tax imposed upon mineral or natural resource production including an ad valorem tax or a gross receipts tax.” H.R. CONF. REP. NO. 95-1752, 95th Cong., 2d Sess. 91 (1978).

The two characteristics of a tax recoverable under § 110, in the view of the Producer Petitioners, are that its calculation is directly related to the rate of current production and that its non-recovery would operate as a disincentive to produce. It is not necessary that the tax be attributable exclusively to production, nor that it be computed in the same manner as a severance or production tax; it is enough that the assessed liability be to some extent “attributable to the production of . . . natural gas.” The Producer Petitioners claim that the FERC’s interpretation—under which the tax must be (1) laid upon “the act of severing,” (2) “each Mcf or MMBtu of gas production,” and (3) assessed “at the time of removal,” *Colorado Interstate Remand Order*, 65 FERC at 62,370, 62,371—effectively reads the term “similar tax” out of the statute.

Applying their more liberal construction of § 110, the Producer Petitioners contend that the Kansas tax fully satisfies the criteria for recoverability. First, while the tax is also

affected by variables other than production, the amount of the tax increases or decreases as production increases or decreases. For example, as between two wells with the same reserves, the one expected to produce more gas will be taxed at a higher level. This argument, however, does little to dispel our understanding that the Kansas tax is by its terms a tax upon property. The value of a depletable asset is a function of its physical and its temporal dimensions; in the case of a gas well, these are respectively the volume of recoverable reserves and the timing of their recovery, which progressively depletes the reserve. The greater the volume of gas produced in a given tax year, the shorter the time over which all the proceeds will be realized and, consequently, the higher the present value of the asset.

The relevant question, therefore, is the obverse of the one suggested by the Producer Petitioners. We do not ask whether two wells with the same reserves would be taxed differently based upon their different anticipated rates of production; obviously they would be, whether the tax is imposed *ad valorem* upon property or upon production. The value of the reserves would be higher for the well with more rapid production because faster production reduces the time over which the flow of gas is turned into a stream of cash. Instead, we must inquire whether the same tax would be levied upon two wells with different reserves but the same level of production. If the tax is based upon production, then the amount of the tax would be the same; if the tax is based upon property, then the amounts would be different. By this criterion, as we shall see, the Kansas tax is laid upon property, not upon production.

In *Colorado Interstate* we posited that the high initial level of production caused by the pressure in a new well could, when annualized in accordance with Kansas's method of appraisal, yield a higher tax upon a property that started operation late in the year than upon an equally productive property that was in operation for the full year. 850 F.2d at 773. Prompted by that observation, the Producer Petitioners now attempt to explain that the State's use of an annualized figure for production when a new well operates for only part



of its first tax year does not relax the relationship between the amount of the Kansas tax and the volume of production. To the contrary, they point out that a 1980 amendment to the Kansas tax law was designed to offset the disproportionately high levy on a well in operation less than six months during the tax year by reducing its appraised value by 40 percent.

Again, the Producer Petitioners' argument supports not their position but the Commission's. As the agency properly observes, an adjustment for the exaggerated level of initial production caused by the high pressure in a new well would be unnecessary if the Kansas tax were indeed based upon production. Any gas produced would be taxed; any gas left in the ground would not be taxed. Kansas authorized an adjustment precisely because its tax is based not upon production but upon gas in the ground; *i.e.*, the State needed a reliable estimate of "annual" production to use in calculating the present value of recoverable reserves. Otherwise there would have been no need to annualize the partial year's output from a new well.

The Commission gave three reasons for rejecting the "measurably attributable to production" standard suggested by the Petitioners. First, it is just the type of murky standard that this court had criticized in *Colorado Interstate. Colorado Interstate Rehearing Order*, 67 FERC at 61,654. Second, the standard is cumbersome to administer; it requires "virtually well-by-well analysis to ascertain exactly how much weight the state property appraiser gave to current production." *Id.* at 61,654-55. Third, simply providing that a tax be measurably related to production does not distinguish between a severance tax and an array of other taxes—income, personal property, real estate—that could vary "in a more-or-less direct manner with production." *Id.*

What is required, contends the Commission, is that the tax vary "directly" with production on "essentially" a one-to-one basis. *Colorado Interstate Rehearing Order*, 67 FERC at 61,655. Indeed there is some support for that proposition in the history of § 110. In 1974 the Federal Power Commission interpreted the Natural Gas Act to allow recovery of the

Kansas tax. Opinion No. 699-D, 52 FPC at 915-16. As we observed in *Colorado Interstate*, however, when the Congress enacted § 110 it supplemented the FPC's formula for recovery ("all . . . production, severance, or similar taxes," Opinion No. 699, 51 FPC at 2301) with the added requirement that the tax be "imposed on the production of natural gas." 850 F.2d at 772. That new qualification is the basis upon which the Commission argues for a one-to-one relationship between the volume of production and the amount of the tax.

The Kansas tax, according to the FERC, is a property tax levied upon the value of recoverable reserves, gas well equipment, and materials, *id.* at 62,374; current production is only a "yardstick by which the value of the leasehold is measured," *id.* at 62,371-72. The appraised value of the reserves depends upon the estimated future production of the well (as determined in part by actual production over the most recent three- or five-year period) and market prices, reduced by operating costs, all forecasted over the probable period of production and discounted to present value. *See Colorado Interstate*, 850 F.2d at 771. Because of differences in the anticipated rate of production and in the estimated quantity of reserves, the tax upon two wells producing the same volume of gas may "vary nearly by a factor of ten." *Id.*

At oral argument, we asked counsel for the Producer Petitioners whether in practice the tax on a well varies over time in direct relation to the well's production. If not, the tax could not properly be characterized as being based upon production. Because the answer to this question has important implications, we take a moment to examine the mechanics of the tax calculation in somewhat greater detail.

The value of recoverable reserves, for the purpose of the Kansas tax, is based predominantly upon the value of the well's average production multiplied by a "present worth factor." The present worth factor, in turn, depends upon the estimated quantity of the reserves, the time value of money, the expected rate of change in the price of gas, and the expected rate of change in production. The Kansas Department of Revenue promulgates a present worth factor for use

in valuing all properties in a major proven gas field. Assuming that the Department determines present worth factors *ex ante* and does not revise them periodically, then the only variable affecting the annual appraisal of a well is the value of the well's production. Under these circumstances, the Kansas tax would, in our view, be sufficiently like a tax "imposed on the production of natural gas" to be recoverable under § 110. Although the tax is called an *ad valorem* tax and calculation of the tax is based upon the present value of recoverable reserves, any change in the amount of the tax due would depend in practice entirely upon a change in the value of production from year-to-year.

The question, therefore, becomes whether there is a change over time in the present worth factor for a particular well or field. If so, then the tax will depend upon the magnitude of that change (and upon any variation in production, of course). In fact, because increased production diminishes the remaining recoverable reserves, and thus typically reduces the anticipated life of a well, periodically updating the present worth factor could yield a tax that is completely unrelated to, or even negatively correlated with, production. Counsel for the Producer Petitioners was not able to refer us to any evidence in the record indicating that the present worth factor for a single field remains constant over time. Therefore, the Petitioners could not show that the Kansas tax necessarily varied in direct relation to production.

Because the Producer Petitioners bear the burden of showing that the Commission's analysis of the Kansas tax is unreasonable, their inability to demonstrate that the present worth factors are invariant over time could have been an end to the matter. Nonetheless, we searched the record independently—but the result was only to increase our confidence that variables other than production can have a material impact upon the tax assessed. Tables captioned "Major Proven Gas Areas and Fields" show a substantial change in the present worth factor for certain fields over the three years from 1986 to 1989. Indeed, the prevailing pattern is for the present worth factor to decline with the passage of time, which is what we would expect. As the anticipated life of a

well declines, the present value of the recoverable reserves decreases correspondingly; that is consistent with our hypothesis that higher production foreshadows a diminished remaining life, which in turn can result in not a higher but a lower tax.

There is more. One appraiser for the Kansas Department of Revenue has identified seven factors other than current production that he considers in determining the present value of reserves: age of the well; quality of the oil and gas; nearness to market; operating costs; character, extent, and permanency of the market; probable life of the well; and the number of other wells being operated. Furthermore, Kansas assesses the tax upon each physical unit of reserves, year after year until the unit is produced. In order to qualify as a severance or production tax under § 110, however, a physical unit must be taxed only once—at the time of production. *Colorado Interstate Remand Order*, 65 FERC at 62,371. The Commission also observes that a typical well in the Permian Basin, roughly 2800 feet deep, will be appraised at a value that includes \$56,000 for equipment alone, *i.e.*, exclusive of the value of any gas reserves. Even after a well has been shut-in for two years the equipment on a “normal” well is valued at \$4,200. If the Kansas tax were based upon production, then there would be no tax on a non-producing well.

Singly and cumulatively, the Commission’s arguments are convincing and neither of the Producer Petitioners’ two principal contentions persuade us otherwise. First, the Producer Petitioners contend, mistakenly, that non-recovery of a property tax based in part upon production operates as a disincentive to produce and thus defeats a primary objective of the NGPA. If the present value of reserves is computed by the Kansas formula, then (other things being equal) the higher the tax rate the greater the incentive to produce. Although higher production is a factor tending to increase the Kansas tax this year, it reduces the expected future production from the well, a factor tending to decrease the Kansas tax in all future years. The tax-reducing effect of decreased life expectancy will almost always exceed the tax-increasing effect of

higher production.\* In short, if demand is inelastic (as it would be when the ceiling is well below market price), a recoverable tax would have little effect upon production at the margin; but a non-recoverable tax would be an incentive to extract gas more rapidly in order to minimize the impact of the tax.

Second, the Petitioners advance the theory (in their Reply Brief) that “a tax qualifies for reimbursement under § 110 . . . if production is a factor in the calculation.” By that standard, an ordinary property tax would qualify as a tax on production; the value of any asset is, after all, the present worth of the benefits that the asset is expected to produce—whether impounded in an established market price or estimated by an appraiser. The Commission reasonably declined to adopt a standard—overbroad, administratively cumbersome, and almost infinitely elastic—with so little to recommend it.

Weighing the various arguments—and mindful that as we said in *Colorado Interstate*, “any Commission interpretation of § 110 that is not precluded by the statutory language and traditional methods of statutory construction, and that is reasonable, will control,” 850 F.2d at 774—we conclude that the FERC’s interpretation of § 110 of the NGPA is reasonable. Furthermore, applying that interpretation, the Commission reasonably determined that the Kansas *ad valorem* tax is not a severance tax within the meaning of that section.

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\* Suppose, for example, a well with 1,000 Mcf of reserves at yearend 1995 is taxed at the rate of \$1 per Mcf remaining on December 31 of each year. The producer would have an incentive to deplete the well as quickly as possible. Production of 500 Mcf on January 1 of both 1996 and 1997 would mean tax assessments of \$1,000 and \$500 on December 31 of 1995 and 1996 respectively. By comparison, production of 250 Mcf on January 1 of each year from 1996 through 1999 would mean tax assessments of \$1,000, \$750, \$500, and \$250 on December 31 of each year from 1995 through 1998—and a much higher total tax. (This assumes of course that the estimated volume of reserves does not change from year to year except to account for the previous year’s production.)

*B. The Colorado and Wyoming Taxes \**

The MPSC, while agreeing with the Commission's interpretation of § 110, urges that the FERC incorrectly applied its own criteria when it allowed recovery of the Colorado and Wyoming taxes. In the *Williams Order*, the Commission stated that "the Wyoming *ad valorem* tax qualifies for recovery . . . in that it is assessed on the volume or the value of the gas which is produced rather than upon the value of gas reserves or lease-hold property. Hence, the tax varies directly, and exclusively, with actual production." 69 FERC at 62,408. The Commission adopted the same rationale in deciding that the Colorado tax could be recovered under § 110. *Id.* at 62,410. The MPSC asserts that this rationale conflates a production-based tax with a property tax.

According to the MPSC, the Wyoming and Colorado taxes are based upon proceeds, not upon production. Taxing authorities administer a proceeds tax as they do a property tax: the underlying property is placed on both state and local tax rolls and aggregated with other property to determine the appropriate state and local *ad valorem* tax rates. A production tax, by contrast, is a state-wide levy subject to a single state-wide rate, administered by and for the benefit of the state and not of the locality. The MPSC contends that the Wyoming and Colorado taxes differ from a typical property

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\* The Indicated Producers claim that the MPSC is barred from contesting the Colorado and Wyoming taxes because the MPSC was some hours late in filing its request for rehearing the *Williams Order*. The FERC, however, waived the 30-day limit in the NGPA, 15 U.S.C. § 3416(a)(2), and accepted the MPSC request as timely filed, *Williams Rehearing Order*, 70 FERC at 61,633. The Indicated Producers argue that the FERC had until then consistently treated the 30-day limit as a jurisdictional requirement that it could not waive. The MPSC replies that the Indicated Producers failed to request rehearing of the Commission's decision to waive the time limit, and thereby failed to preserve the issue for judicial review. We agree. See 15 U.S.C. § 3416(a)(4) (no judicial review unless issue raised before agency in application for rehearing). We proceed therefore to address the question whether the Colorado and Wyoming taxes were recoverable under § 110.

tax only in that they grant a preference to natural gas property over other types of property. In Wyoming, the preference arises by taxing gas property only once, which is to say when the gas is extracted. In Colorado, gas reserves are taxed annually but their value is assumed to equal a specified percentage of the value of the prior year's production. Otherwise, according to the MPSC, the Wyoming, Colorado, and Kansas taxes are similar and ought to be treated similarly under § 110; the Wyoming and Colorado legislatures may be free to favor gas producers over other property owners, but the Congress did not intend to favor gas producers in states with a tax based upon proceeds over gas producers in states that impose upon them a traditional property tax.

The Commission responds, first, that the Wyoming *ad valorem* tax meets the criteria set forth in the *Colorado Interstate Remand Order* and applied in the *Williams Order*, 69 FERC at 62,408. The tax is assessed upon the volume of gas removed from the well, Wyo. Stats. § 39-2-208; payable "one time only . . . as a result of production," *Union Pac. Resources Co. v. State*, 839 P.2d 356, 372 (Wyo. 1992); and based upon the "full value" of the gas when produced, *id.* at 372 n.7. Second, that the tax may benefit local taxing units is not pertinent; a tax imposed "by any political subdivision of a State" is recoverable under § 110. 15 U.S.C. § 3320(c)(2). Third, as this court has recognized, "a tax nominally on property may be functionally identical to a production tax," *Colorado Interstate*, 850 F.2d at 772. Fourth, a tax need not be labeled a "severance tax" in order to be "recoverable" within the meaning of § 110; the term "severance tax" is to be "construed broadly," and may include an *ad valorem* tax, H.R. CONF. REP. No. 95-1752 at 91, as well as any "similar tax, fee, or other levy imposed on the production of natural gas," 15 U.S.C. 3320(c).

Finally, the Commission argues that administrative differences between a tax based upon production and an *ad valorem* tax are irrelevant to the question whether the tax may be recovered under § 110. Indeed, Wyoming has a separate severance tax, which no one here doubts is recoverable within

the meaning of § 110. In distinguishing that tax from the state's *ad valorem* tax based upon proceeds, the Wyoming Supreme Court observed: "[T]he severance tax is an excise tax upon the current and continuing privilege of extracting minerals. . . . An *ad valorem* tax is a property tax which taxes the value of the minerals produced." *Wyoming State Tax Comm'n v. BHP Petroleum Co., Inc.*, 856 P.2d 428, 434 (1993). This characterization of the Wyoming *ad valorem* tax supports the Commission's conclusion that it is based upon production.

Colorado, too, imposes a severance tax in addition to an *ad valorem* tax. The Indicated Producers point out, however, that 87.5% of the *ad valorem* tax may be taken as a credit against the severance tax. This, say the Indicated Producers, proves that the two taxes are "directed at the same activity and intended to accomplish the same purpose, *i.e.*, to tax production as it occurs." Moreover, as the Tenth Circuit noted—albeit in the course of determining whether the Colorado tax is a real estate or a personal property tax, not whether it is sufficiently similar to either a severance or other production-related tax to be recovered under § 110—"[p]ast production is used in the Colorado *ad valorem* tax system only as a gauge for the valuation of the mineral interest. Use of this admittedly imperfect gauge does not rule out the conclusion that the mineral interest itself is being taxed." *Federal Land Bank of Wichita v. Board of County Comm'rs*, 788 F.2d 1440, 1442 (1986).

The Commission nonetheless argues persuasively that the Colorado *ad valorem* tax "varies directly with production" and is "assessed only against gas that is severed from the ground." *Williams Order*, 69 FERC at 62,410. The irreducible fact is that the tax is computed as a set percentage of the market value of the gas removed from a well during the tax year. Colo. Rev. Stat. §§ 39-7-101 and 39-7-102. As we stated in *Colorado Interstate*: When computing the value of property, "[i]f a state sought to capitalize the annual production (or revenue) enjoyed by each producer by multiplying it by a single fixed figure, the [property] tax would plainly be similar enough to a production tax to qualify under § 110."



850 F.2d at 772. That is precisely how the Colorado tax is computed.

In sum, the clear weight of the arguments supports the Commission's determination. Both the Colorado and Wyoming *ad valorem* taxes are based upon production and as such may be recovered under § 110 of the NGPA.

### C. *Retroactivity*

Next we take up the question whether the Commission properly ordered producers to refund Kansas taxes recovered since, and only since, our *Colorado Interstate* decision in June 1988. The governing principle is that when there is a "substitution of new law for old law that was reasonably clear," the new rule may justifiably be given prospectively-only effect in order to "protect the settled expectations of those who had relied on the preexisting rule." *Williams Natural Gas Co. v. FERC*, 3 F.3d 1544, 1554 (D.C. Cir. 1993). By contrast, retroactive effect is appropriate for "new applications of [existing] law, clarifications, and additions." *Id.* The Commission concluded that "[t]he 'settled expectations of those who had relied on the preexisting rule' . . . were changed by the [court's June 1988] *Colorado Interstate* decision, not really [by the FERC's] own decision" in the 1993 *Colorado Interstate Remand Order*, 65 FERC at 62,373.

The Producer Petitioners maintain that the Commission did indeed substitute a new rule for a reasonably clear old rule when, in the *Remand Order*, it first refused to let them recover the Kansas tax. Our decision in *Colorado Interstate*, the Petitioners point out, was a remand, not a reversal, of the Commission's decision in *Sun Exploration* allowing producers to recover the tax. The court directed the Commission only "to exercise its interpretive authority, to identify the features of the Kansas tax that point toward one classification or another, and to offer sensible distinctions between taxes that it chooses to treat differently." 850 F.2d at 775. We did not indicate that we expected a particular result, and consequently we did not disturb the settled expectations of producers who were relying upon the old rule. Upon this view of the

matter, it was precisely the Commission's ruling in the *Remand Order* that did change the governing law; prior to that decision, the Petitioners contend, they did not have reason to anticipate that the Commission would change the rule. As they point out, that the agency had not previously engaged in reasoned decisionmaking did not mean that it could not reasonably reach the same result upon remand. Accordingly, the Producer Petitioners argue that their refund liability should extend back not to June 1988 but only to December 1993.

PSCC, on the other hand, argues that regardless of when the Commission first determined that recovery of the Kansas tax was unlawful, it necessarily had been unlawful since the NGPA was enacted in 1978. After first arguing before the Commission for full retroactivity back to 1978, however, PSCC conceded that "fundamental fairness . . . [dictates] that the date on which interested parties were put on notice of the dispute should control the date of retroactivity." Request for Rehearing, *Colorado Interstate Gas Co.*, Dkt. Nos. GP83-11-003 and RI83-9-004, at 6 (FERC Jan. 3, 1994). Therefore, suggested PSCC, liability for refunds should extend back at most to August 1983, when Northern Natural petitioned the Commission for a determination that the Kansas tax was not recoverable under § 110, or at least to October 1983, when all interested parties received notice of the petition by publication in the Federal Register. *Id.* at 4.\* As between the two, the later date is obviously the correct one. See *Associated Gas Distribs. v. FERC*, 899 F.2d 1250, 1256 (D.C. Cir. 1990) (FERC gives notice of petition by publication in Federal Register).

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\* The MPSC argues for full retroactivity back to 1978, but we agree with the Producer Intervenors that it is precluded from raising that argument before us. The MPSC did not make a retroactivity argument in its request for rehearing before the FERC, and it does so here only as an intervenor, not as a petitioner. See *Illinois Bell Tel. Co. v. FCC*, 911 F.2d 776, 786 (D.C. Cir. 1990) ("An intervening party may join issue only on a matter that has been brought before the court by another party").

To recapitulate, the various parties now urge that when the Commission issued its *Colorado Interstate Remand Order* in December 1993, it should have made liability for refunds (per the Producer Petitioners) prospective-only; (per the Commission) retroactive to June 1988, when we issued our decision in *Colorado Interstate*; or (per PSCC) retroactive to October 1983, when notice of Northern Natural's petition to disallow recovery of the Kansas tax was published in the Federal Register.

PSCC, the MPSC, and the Commission all argue against prospective-only application. By December 1993 gas at the wellhead was no longer subject to a maximum lawful price; deregulation had rendered § 110 moot almost a year before. See Natural Gas Wellhead Decontrol Act of 1989, Pub. L. No. 101-60, 103 Stat. 157. Accordingly, producers would have no liability under a rule that limited refunds to taxes paid on post-December 1993 production. Their point seems to be that customers should not lose their entitlement to refunds merely because the Commission took five years after our decision in *Colorado Interstate* to issue the *Remand Order*.

The FERC makes a more convincing argument against prospective-only application of its 1993 decision based upon this court's criticism in *Colorado Interstate* of both the logical and the factual bases for the agency's prior policy; that sent a "clear signal" to producers that their recovery of the Kansas tax under § 110 might not be lawful. After that "the parties no longer would have been justified in relying on the Commission's earlier rulings with any assurance that they would not later be required to make refunds." *Colorado Interstate Remand Order*, 65 FERC at 62,373.

The Commission marshals the events leading up to the *Colorado Interstate* remand in further support of this compromise view. As we have seen, under the Natural Gas Act, the Federal Power Commission had held in 1974 that the Kansas tax could be added to the maximum lawful rate. Opinion No. 699-D, 52 FPC at 915-16. Four years later the Congress carried forward into the new NGPA a provision nearly identical to the provision of the NGA that the FPC had

earlier applied to the Kansas tax. See Opinion No. 699, 51 FPC at 2301. Furthermore, in the legislative history of the NGPA the Congress specifically anticipated that producers might recover an *ad valorem* tax under § 110. H.R. CONF. REP. NO. 95-1752 at 91. In 1986 the Commission reaffirmed that the Kansas tax was recoverable under that section. See *Sun Exploration*, 36 FERC ¶ 61,093. Not until our 1988 decision in *Colorado Interstate*, remanding *Sun Exploration*, was there any official suggestion that the law might be otherwise. Finally, in 1993 the Commission effectuated a change in the law by developing new standards for determining whether a tax may be recovered under § 110. Thus, according to the Commission, the producers had no indication that the rule might be any different until our *Colorado Interstate* decision in 1988, and requiring them to refund taxes recovered with respect to gas produced prior to that date is not justified.

The agency also concludes that requiring refunds back to the date of our decision in June 1988 properly balances the producers' equitable claim to notice against the consumers' legal right to receive a refund of all unlawfully collected charges. On the one hand, prospective-only application of the law would permit producers to retain sums collected from June 1988 to December 1993 in excess of the maximum lawful prices prescribed in the NGPA—without any supporting rationale. On the other hand, a fully retroactive remedy would penalize producers by requiring disgorgement of sums they innocently collected prior to June 1988—even though our 1988 *Colorado Interstate* decision was the first authoritative indication that the Kansas tax might not be recoverable after all.

In support of making the Commission's decision retroactive to 1983, PSCC offers a different account, or at least one with a different emphasis, of the transition from the NGA to the NGPA. In this version the key point is that the Commission does not have the expansive remedial powers under the NGPA that it wielded under the NGA, 15 U.S.C. § 717c(e). Specifically, whereas the NGA gave the Commission discretion to order refunds if it determined that a rate was not just

and reasonable, the NGPA established maximum lawful prices and gave the customer a right to a refund if it was overcharged.

PSCC also points out that when it issued the *Remand Order* the Commission was not engaged in rulemaking but in adjudicating the rights of the parties before it; therefore the agency was necessarily articulating and giving retroactive effect to existing law. When it is clarifying existing law, rather than substituting new law for old, the agency need not be as attentive "to protect[ing] the settled expectations of those who had relied on the preexisting rule." *Williams*, 3 F.3d at 1554. Indeed, as PSCC points out, the producers never explain how their "settled expectations" led them into detrimental reliance upon being able to recover the Kansas tax.

As we see the issue, the apparent lack of detrimental reliance on the part of the producers is the crucial point. What would they have done differently if they had known in 1983 that they were not entitled to recover the Kansas tax? They could not have raised their prices above the maximum lawful level regardless whether the traffic would have borne such an increase. Nor do they contend that existing prices were below the lawful limit; and if they were, price increases might still have been foreclosed by competitive constraints. The producers may have shut in some wells or refrained from exploring for new wells if their inability to recover the tax would have rendered the wells unprofitable, but neither the producers nor the Commission has even suggested these possibilities. All the producers do suggest is that "[a] prudent producer would have cut back on production to the extent that non-recovery of the tax increased [the] current marginal cost of production," *Petition of Producer Petitioners for Rehearing of Order on Court Remand, Colorado Interstate Gas Co.*, Dkt. Nos. GP83-11-003 and RI83-9-004, at 23 (FERC Jan. 3, 1994), but in this they are mistaken; as noted above, the more slowly a well is depleted, the greater the remaining reserves and the higher the tax thereon. Moreover, neither party has even roughly quantified the harm (*e.g.*, the expenditures made and lost in detrimental reliance

upon being able to recover the Kansas tax) that the producers might suffer should they have to refund the full amount that they unlawfully collected. In these circumstances, we are hard pressed to see how the producers would be harmed in any cognizable way even if they were required to disgorge every dollar they received in recovery of the tax (assuming any party were seeking such extensive relief).

Not only is the producers' "detrimental reliance" purely notional; if it were real it would not have been reasonable. The enactment of a substantially new regulatory regime in 1978 undermined any assurance that the FPC's treatment of the Kansas tax under the NGA would withstand scrutiny under the NGPA; reliance would have been foolhardy. If that were not enough, the status of the Kansas tax was expressly drawn into question in 1983 when Northern Natural first petitioned the Commission for a ruling that producers could not lawfully recover the tax under § 110. Once the recoverability of the tax was in dispute, we do not see how the Commission could possibly find that producers reasonably relied upon continuing to recover it.

Because no seller of natural gas could justifiably be confident that it was entitled to recover the tax until the legal question was settled anew under the new statute, we hold that the producers' liability for refunds extends back to October 1983, the date when all interested parties were given notice in the Federal Register that the recoverability of the Kansas tax under § 110 of the NGPA was at issue, and the earliest date advocated by any party before this court. Absent detrimental and reasonable reliance, anything short of full retroactivity (*i.e.*, to 1978) allows the producers to keep some unlawful overcharges without any justification at all. The court strongly resists the Commission's implication that the Congress intended to grant the agency the discretion to allow so capricious a thing. Still, we do not require refunds of taxes recovered with respect to production before October 1983 because there is before us no controversy over those monies.

*D. The Pipeline as Guarantor*

In the *Colorado Interstate Remand Order* the Commission required interstate pipelines to “pass through any *ad valorem* tax refunds they receive from first sellers,” 65 FERC at 62,374, but made it clear that “pipelines will not be required to be guarantors of refunds.” *Id.* The MPSC, on behalf of the customers of the Williams pipeline, was the only party to challenge that decision. The FERC adhered to its position, however, adding that Williams should not be treated differently than other similarly situated pipelines. *Williams Natural Gas Co.*, Dkt. Nos. TA89-1-43-004 and RP89-39-005, slip op. at 5 (FERC order June 2, 1994), *clarification denied, Williams Order*, 69 FERC ¶ 61,373. The MPSC properly dispatches the FERC’s afterthought with the observation that it is routine for one pipeline to be required to make refunds while others are not—because the one is challenged and the others are not.

In its petition for review, the MPSC raises three objections to this aspect of the Commission’s decision. First, it observes that under § 4 of the NGA the Commission is authorized to order refunds of any amounts collected from consumers in excess of what is just and reasonable. 15 U.S.C. § 717. Second, the MPSC contends that until the *Colorado Interstate Remand Order* was issued in December 1993, Williams should have understood that when it was allowed to continue collecting from its customers the amount of the Kansas tax “subject to refund,” it became conditionally obligated to refund any amount later determined to be unlawful. Indeed, Williams received explicit notice in 1989 that the Commission was considering whether monies collected in recovery of the Kansas tax would have to be refunded. *Williams Natural Gas Co.*, 47 FERC ¶ 61,114 at 61,341. According to the MPSC, this notice should have prompted Williams to take reasonable steps to assure that it could in turn obtain refunds from its suppliers. Third, the MPSC asserts that the Commission should have required Williams to put the monies it received for the Kansas tax into escrow (or post a bond or obtain a letter of credit) in order to assure their return if need be. Escrow arrangements are commonly used when a

rate increase is conditionally allowed to take effect until the agency determines whether it is lawful. *See, e.g., Transcontinental Gas Pipe Line Corp. v. FERC*, 866 F.2d 477, 479 (D.C. Cir. 1989).

The Commission responds, first, that there is well-established precedent for treating pipelines as mere conduits for the flow of refunds from producers to consumers. *See, e.g., Public Utils. Comm'n of Cal. v. FERC*, 24 F.3d 275, 278 (D.C. Cir. 1994). Second, the FERC explains that accepting Williams' rates "subject to refund" means simply that the agency would order refunds if appropriate after the remand proceedings in *Colorado Interstate*, not that Williams was expected to pay the tax monies into escrow (or take equivalent steps) in order to assure that they would be available if refunds were ordered. Third, the Commission maintains that it could not have directed Williams to set up an escrow arrangement because the pipeline was obligated by contract to pay producers the amount of the Kansas tax. The Commission points to § 601(c) of the NGPA, 15 U.S.C. § 3431(c), which guarantees a pipeline full recovery of its gas purchase costs.

The Commission's arguments are not convincing. Surely Williams' contractual obligation does not extend to paying to producers sums unlawfully recovered. While § 601(c) requires that a pipeline be allowed fully to recover its gas purchase costs, that provision also authorizes the Commission to deny recovery of costs that are unjust or unreasonable. Moreover, the Commission would not have violated § 601(c) by requiring that the taxes be placed in escrow while the agency determined whether they could indeed be recovered under § 110. An escrow arrangement would have preserved the rights of all parties. If the Commission ultimately decided that the taxes were recoverable under § 110, then the producers would be entitled to the amount in escrow, including any accrued interest. If, as happened, the Commission decided that the taxes were not recoverable, then the amount in escrow could have been refunded to the ratepayers (again, with interest). In either event, the pipelines would have recovered their full gas purchase costs.



Regardless whether the Commission abused its discretion by failing to require an escrow or its equivalent—a matter we need not decide today—the MPSC's petition for review must be denied. Insofar as it seeks prospective relief, the issue is moot: Wellhead prices have been totally deregulated since 1993, there are no longer any maximum lawful prices for producer sales, and whether a producer recovers severance taxes is a matter of negotiation between buyer and seller. As for monetary relief, it is too late now for the Commission to require that Williams pay the severance taxes into escrow; the pipeline has long since paid the monies to the producers.

Nor does the MPSC make out any legal or equitable principle that would suggest holding Williams accountable for the Commission's failure to protect consumers. The pipelines were, as the Commission has reminded us, mere conduits; they had no financial interest in this dispute. The Commission's failure to impose an escrow or other arrangement did not benefit the pipelines, and it is not clear why they should be at risk because the FERC may have been remiss. Nor was Williams obliged either by contract or by regulation to take any precaution against the possibility that a producer would fail to refund monies due to consumers. Therefore, there is no ground upon which the court can say that the Commission was required to hold the pipeline—which was charged first with the task of collecting tax payments and then of distributing tax refunds—liable if the responsible producer defaults on its refund obligation.

### III. Conclusion

The Commission's interpretation of § 110 of the NGPA is in all respects reasonable. The Commission properly rejected the Producer Petitioners' proposal that it allow recovery of any tax that was "measurably attributable" to production. That standard is overbroad and unwieldy, and we criticized it as ambiguous in *Colorado Interstate*. The agency reasonably determined that the Kansas *ad valorem* tax is not a severance tax within the meaning of § 110. The Kansas tax is a function of numerous factors other than production, with the

result that producers of equal volumes of gas may be taxed very different amounts; and the tax falls upon each unit of reserves each year, rather than once at the time of extraction. Further, the Producer Petitioners are mistaken in their assertion that non-recovery of a property tax based in part upon production is a disincentive to produce.

The Commission reasonably determined that both the Wyoming and the Colorado *ad valorem* taxes were recoverable as severance taxes under § 110 of the NGPA. The Wyoming tax is assessed upon the volume of gas removed from the well; it is a "one time only" tax, based upon the value of the gas when produced. That the state treats the tax as a property tax is of no moment if, in the terms of § 110, it is "imposed on the production of natural gas." 15 U.S.C. 3320(c). The Colorado tax, also administered as a property tax under state law, is computed as a set percentage of the market value of the gas removed from a well during the tax year. That is "plainly . . . similar enough to a production tax to qualify under § 110." *Colorado Interstate*, 850 F.2d at 772.

Producers are liable to refund all Kansas *ad valorem* taxes collected with respect to production since October 1983. An agency adjudication should be applied retroactively unless new law is replacing clearly defined old law and reasonable reliance interests must therefore be protected. Here the agency did not change the law—rather, the Congress did when it enacted the NGPA in 1978—nor was there any showing that the producers had relied, let alone detrimentally or reasonably relied, upon the continuing validity of the agency's interpretation of the NGA. There is no substantive reason, therefore, to deny customers all the relief to which they are entitled. The customers are limited, however, to recovery of taxes paid with respect to production since October 1983 because that is the earliest date for which any argument has been preserved in this proceeding for review.

Finally, the court will not require the Commission to make the Williams pipeline a guarantor of the producers' obligation to refund the Kansas tax. Although an escrow arrangement would likely have preserved the rights of all parties, the

Commission did not impose one, and no party has pointed to any legal or equitable principle by which the agency can be required to hold a pipeline accountable for the agency's own oversight.

For these reasons, we deny the petitions for review filed by the Missouri Public Service Commission and the Producer Petitioners, and we grant the petition for review filed by the Public Service Company of Colorado.

*So ordered.*

SENTELLE, *Circuit Judge, concurring*: I join without reservation in the holding of the court. I write separately only to place a little distance between myself and what I deem to be an overstated dictum. After describing a hypothetical tax, the majority states that with the majority's proposed variations "the Kansas tax would, in our view, be sufficiently like a tax 'imposed on the production of natural gas' to be recoverable under § 110." Maj. op. at 11. As no such tax is before us, for us to authoritatively render an opinion on what it would be constitutes nothing less than the advisory opinion that Article III courts have held ourselves unable to render since the earliest days of constitutional jurisprudence. *See, e.g., Flast v. Cohen*, 392 U.S. 83, 96 (1968) ("[T]he oldest and most consistent thread in the federal law of justiciability is that the federal courts will not give advisory opinions." (Internal quotations and citations omitted)); WRIGHT, MILLER & COOPER, 13 FEDERAL PRACTICE AND PROCEDURE § 3529.1 (1984) (detailing the long history of the rule forbidding advisory opinions). We have already, in my view, crossed the line of appropriate Article III jurisprudence in dealing with § 110 tax treatment when the prior panel stated "[i]f a state sought to capitalize the annual production (or revenue) enjoyed by each producer by multiplying it by a single fixed figure, the [property] tax would plainly be similar enough to a production tax to qualify under § 110." *Colorado Interstate Gas Co. v. FERC*, 850 F.2d 769, 772 (D.C. Cir. 1988). I think it time we quit advising state legislatures on how to draft their tax statutes and confined ourselves to construing the statutes actually before us.

Mr. BARTON. The Chair is going to recognize himself for 10 minutes for questions.

The Chair first wants to say that the Chair has read the Constitution and sees that there are three equal branches of government and one of them is the legislative branch and the legislative branch has the right and opportunity to take issue of what the judicial branch does.

Quite frankly, I don't give a hoot what the D.C. Court of Appeals ruled since I am not an attorney and I am not a judge but I will have to admit that they ruled in your favor or your clients' favor, Mr. Albright.

I do want to go to the Attorney General from Kansas and I want to get the record straight about what the issue is. In 1978, we passed a Natural Gas Policy Act, the Congress did, which regulated a wide range of natural gas prices that heretofore had not been regulated and they did set a maximum lawful ceiling price for a number of categories in natural gas.

My assumption is that most of the gas contracts that are in question in this litigation were old gas contracts under the definition of the Natural Gas Policy Act of 1978; is that correct?

Ms. STOVALL. That would be my understanding, but I don't have that historical perspective. What I would offer though, from 1954 the Federal Government has had the ability to regulate gas at the wellhead so you had that even before the Natural Gas Policy Act.

Mr. BARTON. Interstate sales not intrastate sales. You couldn't regulate natural gas prices intrastate until the Natural Gas Policy Act of 1978. I used to be the natural gas deregulation consultant for Atlantic Richfield Oil and Gas Company so I am a little hazy on this, but it is still back there somewhere.

Ms. STOVALL. You at least had it there and I didn't. You can be our expert on that issue then.

Mr. BARTON. Kansas at the time the NGPA came in effect in 1978 had an ad valorem tax, not a production tax; is that correct?

Ms. STOVALL. That is true.

Mr. BARTON. There was a Federal Power Commission or Federal Energy Regulatory Commission, which was a successor to the Federal Power Commission, ruling that said the Kansas ad valorem tax could be passed through as an add-on to the maximum lawful ceiling price; is that correct?

Ms. STOVALL. You are absolutely right. In 1974, opinion number 699 and 699-D from FERC said exactly that.

Mr. BARTON. Because the gentlelady from Missouri made some statements in her very precise soft voice about unlawful prices, technically she is correct after the fact. She wasn't completely correct because, at the time, there was a ruling that you could sell at a regulated price. The Federal Government or an agency of the Federal Government set the regulated price.

The State of Kansas under the constitution has the right to have State taxes, and they had an added value tax, an ad valorem tax, not a production tax, not a severance tax but an ad valorem tax. FPC or the FERC said that can be passed through; is that correct?

Ms. STOVALL. You are exactly right.

Mr. BARTON. So Kansas got its taxes. The taxes were paid.

Ms. STOVALL. True.

Mr. BARTON. But the pipelines who bought the gas paid the taxes because at that time most pipelines took ownership of the gas that they purchased; is that correct?

Ms. STOVALL. That is correct.

Mr. BARTON. Now, the great FERC represented by the general counsel here, Mr. Smith, who ruled, I am told, five times that what Kansas was doing and what Kansas producers were doing was legal came back and when the case went to the D.C. Court in 1988 and the D.C. Court said, well what FERC has ruled we don't think is right and they remanded that to the FERC. And 5 years later the FERC said, well, we guessed what the District Court said is correct and what we have said all along is wrong. Is that correct?

Ms. STOVALL. Basically. If I could add something. In 1988 when the D.C. Circuit remanded it back, it wasn't to say we don't think FERC made the right decision. It was simply to say their decision fell short of explaining properly how they classified the Kansas tax.

Mr. BARTON. The D.C. Court didn't rule in favor of, I would say, the plaintiff. The D.C. Court just said the FERC needs to take another look at this.

Ms. STOVALL. And explain it better.

Mr. BARTON. And after 5 years, the FERC decided that they were wrong, that they had ruled the wrong way all these other times.

Ms. STOVALL. That is correct.

Mr. BARTON. Now, do you know of any attorney in oil and gas practice in the great State of Kansas who, before the D.C. Court remanded it back to the FERC, would have said that it was unwise, unsound, imprudent to rely on the five previous FERC or FPC rulings?

Ms. STOVALL. I know of no oil and gas lawyer in Kansas that would have given that advice.

Mr. BARTON. At that time.

Ms. STOVALL. True.

Mr. BARTON. At that time.

Now, Mr. Smith, you said in your written testimony that the FERC takes no position on the legislation that Mr. Moran has introduced. It says neither the Commission as a whole nor Chairman Hoecker has taken a position on the legislation proposal.

Now, in a letter to the Chairman of the Appropriations Committee which, according to the facts that I have, is dated April 15, 1999, says this note responds to your request for Chairman Hoecker's views on section 2316 of H.R. 1141, the fiscal year 1999 Emergency Supplemental Appropriation Act, the chairman would not oppose enactment of this amendment. Are you cognizant of this particular document?

Mr. SMITH. Yes.

Mr. BARTON. So when I read the chairman would not oppose enactment of this amendment if it is not identical it is very similar to Mr. Moran's legislation, that the FERC would not oppose enactment of Mr. Moran's legislation; is that correct?

Mr. SMITH. As you may be aware, we provided that note in response to an appropriations staff request for our views on this subject. Almost instantaneously, we were asked questions by third parties who saw that version of the statement and said, well, does this mean that the chairman supports the slightly different provision

that was being discussed in the context of the supplemental appropriations bill. That was clearly not our intent.

The chairman's intent was to state a view of neither opposing nor supporting that legislation, and when we received written questions from the Appropriations Committee in connection with their review of our budget which asked the same question, we made that clarification, that the chairman——

Mr. BARTON. Let's clarify for this subcommittee your position on Mr. Moran's legislation. You are not a commissioner at the FERC, but you are the general counsel. Can I characterize the FERC's position is that they don't oppose the Moran bill?

Mr. SMITH. We don't oppose and don't support. We have taken no position as my testimony said.

Mr. BARTON. You are not opposed to it. You are not going to be upset if we mark this up in subcommittee within the next month and send it to the full committee?

Mr. SMITH. Well, I can't speak for when the commission will get upset but yes, that is right, we have carefully not taken a position.

Mr. BARTON. How long have you been at the FERC?

Mr. SMITH. A year and a half, roughly.

Mr. BARTON. Before you came to the FERC in your current capacity, you weren't at the FERC in some other capacity?

Mr. SMITH. No.

Mr. BARTON. So you are not aware of the thinking of the Commission at the time they reversed their position?

Mr. SMITH. Only as evidenced by their written orders.

Mr. BARTON. Can you summarize quickly why they flip-flopped on this? Because if they had not, none of this would be an issue.

Mr. SMITH. As you are aware, the Commission in 1983 got a request from a pipeline to reconsider its pre-NGPA position that these Kansas ad valorem taxes should be recoverable. As far as I am aware, there were only two FERC decisions in response to that, the initial order in the case and the order on rehearing, both of which found that the Kansas ad valorem tax could be treated as recoverable under section 110.

Then in 1988 the D.C. Circuit critically reviewed the Commission's reasoning, focusing on two aspects of it. First, was there sufficient reasoning or explanation generally of the commission's decision. And second, could the Commission distinguish its position concerning the Kansas ad valorem tax from its position on the Texas ad valorem tax, which the Commission had consistently treated as not a tax on production and not recoverable under section 110.

And in that remand, the court instructed the Commission to go back and give a rigorous review of how it was going to distinguish between property taxes and production taxes. In doing that review based on the discussion in the D.C. Circuit decision and the other issues that were discussed in the 1993 order, the Commission reversed its view.

Mr. BARTON. My time has expired. There is a difference between Texas and Kansas I believe. In Texas, we have severance taxes, and we had ad valorem property taxes. But in Kansas I think they just had the ad valorem tax. I don't think they had a severance tax.

Mr. SMITH. At that time.

Mr. BARTON. So there was that distinction. My time has expired. The Chair is going to recognize the gentlelady from Missouri for 10 minutes.

Ms. MCCARTHY. Thank you for your generosity, Mr. Chairman.

Mr. BARTON. I recognized myself for 10 minutes. I have to be fair.

Ms. MCCARTHY. I would like to ask the Honorable Ms. Stovall a question. I am going to put my Ways and Means cap on. This is on taxes since Mr. Barton mentioned the Kansas tax situation. The tax in question is the Kansas State tax; and ultimately, the revenues from this tax ended up in the Kansas treasury. Why then hasn't the State of Kansas offered to reimburse producers for the cost of refunds using the original tax moneys plus the interest earned over the years?

Ms. STOVALL. Again, Kansas doesn't have that money set aside just like the producers don't have that money set aside. Kansas takes the position that the producers lawfully collected that amount that they were entitled to do and it has been utilized for purposes in the State of Kansas.

Kansas doesn't think it is our obligation to give it back. We think that we lawfully collected it under the laws of FERC at that time.

Ms. MCCARTHY. Given all the testimony we have heard today, I am surprised that Kansas didn't set it aside in some sort of fund but also given a sense that most States are in surplus right now and budget surpluses because of the great economy. I also find it difficult to understand how Kansas wouldn't—having used this State tax not find it good on a solution because my understanding is, and I am looking at the Missouri data and some things that Mr. Albright said, Kansas people, the people of Kansas as well as the Kansas-based pipelines, the rate payers in the pipelines, there is \$82 million due them.

Who in Kansas is advocating for the Kansas-based pipelines and the rate payers? You are here today taking sides with the producers and I understand that, but whose job is it in Kansas to help them get that \$82 million back?

Ms. STOVALL. There is an organization that deals with consumers on utility issues and they have the right to be any place and say what they want. In Kansas, the way we have evaluated it though is the small benefit to the consumers being about the \$15 total is absolutely outweighed by the detriment to the producers and the royalty owners that would come about by having to pay this.

Even though I am charged in my State with enforcing the Consumer Protect Act, I find that the equities absolutely don't support giving this \$15 to the consumers in light of what would happen. Again, those figures that you look at that talk about \$77 million that's absolutely an estimate—

Ms. MCCARTHY. \$82 million.

Ms. STOVALL. \$82 million, whatever it is. There is no certainty and my saying \$77 million and your saying \$82 million indicates we don't know where the numbers have come from. They are simply estimated bills that pipelines have submitted assuming that the pipelines always paid the maximum lawful price in addition to that tax.



The records we have had a chance to look at would suggest that is not true across the board; but because we haven't been given the opportunity, we being the producers and the royalty owners to have a due process hearing, we can't even justify nor respond to what those bills are and yet FERC has said that those producers and royalty owners owe 100 percent already.

Ms. MCCARTHY. It is my understanding that the 85 percent of the money that is due is owed by 24 large companies that are mostly national and international and outside of Kansas. That is who you are speaking of?

Ms. STOVALL. Actually not. What we show is the median claim of the royalty owners is \$22,000. That breaks down to being 12 claims that are under \$100; 97 that range from a \$100 to a \$1,000; 125 claims between a \$1,000 and \$5,000; 76 that range between \$5,000 and \$10,000; and then there are 9 that are over \$10 million.

Ms. MCCARTHY. Those are the Kansas companies you just gave me—

Ms. STOVALL. Those are the producers.

Ms. MCCARTHY. Are those the Kansas producers?

Ms. STOVALL. They are the producers. They are not necessarily all Kansas producers, but they do produce in the State of Kansas.

Ms. MCCARTHY. Can you provide that information for the committee? Because, obviously, the data that Mr. Albright was referring to and the Missouri Public Service Commission presented us is not quite in sync with that information.

Ms. STOVALL. Again, and—this is the information we've been able to put together. The information that Mr. Albright and the Missouri Commission have are supported by the pipelines. That information came from the pipelines which, again, are just very base estimates.

Ms. MCCARTHY. We try to hear from all sides here. That is what is great about this subcommittee.

Ms. STOVALL. I appreciate that.

Ms. MCCARTHY. Commissioner Lumpe, I wonder if you, and, Mr. Albright, you can weigh in on this if you would like, we don't always have the right to legislate everything up here. We may try, but my question is is this legislation constitutional? It seems to alter final judgment by the court. And in my mind may constitute a taking, and I would love your thoughts on that.

Ms. LUMPE?

Ms. LUMPE. I think, Ms. McCarthy, that you are asking me a legal question and not being an attorney, I sort of hesitate to answer that. But I would be happy to try to provide an opinion for you on that, whether the current NGPA Act is constitutional that this would involve a taking.

I would assume that in the challenge that was brought to the court on this and the court's ruling that the refunds were due, that that issue may have been addressed there and that we would then rely on it. But not being an attorney, I really couldn't give you my own take on whether this is a taking.

Ms. MCCARTHY. I would appreciate the thoughts from your attorneys on this because I am quite curious that you and I both have grappled with the issue of takings in our prior lives as legislatures, and we grapple with again here in the Congress. I certainly

wouldn't want to be embracing legislation that would exacerbate that difficult question.

Mr. Albright?

Mr. ALBRIGHT. Yes. If I may weigh in on this, I am not a constitutional lawyer. But we have taken a look at the issue and the fact that years after the right to collection of these refunds were vested, gas consumers are in fact entitled to interest. That is part of the compensation under the American jurisprudence is to receive interest on refunds.

We believe it would wrongfully sidestep the takings clause to enact legislation now that forgives that interest. I think the Natural Gas Policy Act vests exclusive jurisdiction in the courts to resolve these matters too. So to the extent that Congress acts now to take that legislation away and to usurp the rights of parties that have vested rights now, that that would be unconstitutional.

Ms. MCCARTHY. Thank you very much. Mr. Chairman, I thank you and I am going to go vote.

Mr. BARTON. Would the gentlelady yield.

Ms. MCCARTHY. Of course, Mr. Chairman.

Mr. BARTON. We repealed the pricing provisions of the Natural Gas Policy Act. We had not repealed the Act in its entirety, but at the time the pricing provisions were still in effect, the clients that you represent had contracts that gave them the opportunity to purchase this gas. They were aware when they purchased it that part of the fee they were making was an ad valorem tax, were they not?

Mr. ALBRIGHT. The clients I represent are local distribution companies which were customers of the pipelines.

Mr. BARTON. The clients which you represent purchased gas knowing that included in the price were taxes; is that not correct.

Mr. ALBRIGHT. That is correct.

Mr. BARTON. Are you aware of any of your clients, at the time they received the gas to consume the gas or to resell the gas, make an issue, at that time, of not paying the total price they were asked to pay because of this issue?

Mr. ALBRIGHT. Well, Mr. Chairman, for the period in question, I was not even an attorney. I did not represent Public Service Company of Colorado nor Cheyenne Light, Fuel, and Power; but I would like to speak to the issue as being an employee of a gas pipeline company, KN Energy, Inc. And I was in the Kansas gas patch purchasing gas from producers and negotiating contracts with gas producers, and I was very aware of this issue. And our company was very familiar with the litigation that was ongoing and paid close attention to it.

Mr. BARTON. They voluntarily paid a price knowing that part of the price included these taxes.

Mr. ALBRIGHT. That is correct.

Mr. BARTON. For that payment, they received a commodity, i.e., natural gas; isn't that correct?

Mr. ALBRIGHT. That is correct.

Mr. BARTON. They got a good in return for paying a price that included these taxes.

Mr. ALBRIGHT. That is right.

Mr. BARTON. This whole issue goes back to, again, we set a ceiling price and Kansas chose to apply a tax in a different way than

other States, but the tax was paid, the State of Kansas received the tax and now because of the D.C. Court and because of the FERC change of position, there is several hundreds of millions of dollars apparently at issue in taxes that have been paid; is that not correct?

Mr. ALBRIGHT. That is correct, Mr. Chairman.

Mr. BARTON. I thank the gentlelady. Does the gentleman from Arizona wish to be recognized now or do you wish to go vote and come back? We are trying to continue the hearing.

Mr. SHADEGG. I would just as soon go vote and come back.

Mr. BARTON. The gentleman from Texas is recognized.

Mr. HALL. Mr. Albright, how much of a refund would your electric and gas customers—how much would you collect if you were successful in collecting all that is due you from Kansas producers?

Mr. ALBRIGHT. Calculations based on the interstate pipelines from which we purchased gas during this period indicates we would receive approximately \$23 million for our customers.

Mr. HALL. How much would that be per customer?

Mr. ALBRIGHT. We made a rough calculation based on current consumer base, our customer base as it exists now for residential customers, the average refund to each customer would be approximately \$15, and for the average commercial customer the refund would be approximately \$90.

Mr. HALL. What would the State regulators do if you failed to collect these amounts?

Mr. ALBRIGHT. I can't speak for my regulators. Sometimes they are unpredictable. I imagine they would be very upset, but whether they would take any further action—

Mr. HALL. You folks had to make some kind of reserve. What recommendations did you make to them?

Mr. ALBRIGHT. We already received approximately \$2.5 million of refunds for these Kansas ad valorem taxes.

Mr. HALL. You settle with any of them for less than what their average would be? I don't know how you would do that.

Mr. ALBRIGHT. I don't know how we would do that either. The issue is for purposes of rate regulation for local distribution companies, our customer base changes very significantly over time and the way we purchase gas and flow those gas costs through, it is on a dollar-for-dollar basis through an adjustment mechanism we have on our tariffs. The Colorado statutes provide for a low-income fund, a Colorado energy assistance fund which is referred to in one of the letters I submitted this morning.

And that provides for any undistributed amounts of refunds from upstream suppliers to be credited to this fund for purposes of administering the low-income funds. So to the extent the specific customers—existing customers on our system don't get the full allocated average refund, the amounts would go toward the low-income customers.

Mr. HALL. Been able to get the money back to the customers?

Mr. ALBRIGHT. Yes, they would.

Mr. HALL. Have you been able to do that?

Mr. ALBRIGHT. Yes, we have.

Mr. HALL. What is going to be the aftermath of this? What is the effect of this bill if we pass this bill in the present sense?

Mr. ALBRIGHT. To the customers?

Mr. HALL. Yes.

Mr. ALBRIGHT. They won't get \$360 something million dollars they are entitled to under the law.

Mr. HALL. The producers won't pay it.

Mr. ALBRIGHT. And the producers won't pay it.

Mr. HALL. We, a lot of times, try to balance equities up here. I am very pro producer myself. I don't—I will read the testimony. I am sorry I didn't get to hear your testimony, but you have given it to me. I will read it.

Mr. Chairman, I yield back the balance of my time.

Mr. SHIMKUS [presiding]. Thank you. I will recognize myself for as much time as I may consume or until someone else comes back and kicks me out of the Chair.

My opening statement had just the fact that Illinois rate-payers and companies had, based on the dollar amount with the principal and the interest of about \$22 million, \$994,000 due them so I guess I have a couple of questions, and I will just throw this open to the panel first.

Is there a risk that pipelines and local distribution companies will keep a portion of the refund? I know Congressman Moran suggested that that would occur.

Why or why not? Carla?

Ms. STOVALL. We very much know that some of the pipelines have that intention. In fact, two of the pipelines have petitioned FERC to be allowed to keep 100 percent of the refunds and that indeed has happened in ANR in El Paso. It is our information in addition to that, that pipelines who have retail customers, when they sell to big consumers that it is their intention to argue that all that money should be kept by the pipelines because no refund was contemplated in the contracts that they had with those individuals.

And so it is very much the information we have that the amounts of refunds to consumers will be very limited by what the pipelines and/or the local distribution companies intend to keep. The local distribution companies whether or not they can keep any of the money is on a State-by-State basis with the State regulatory agency, and so that will be yet to be determined by those individuals.

Mr. SHIMKUS. Thank you. Anyone want to dispute that?

Mr. ALBRIGHT. Mr. Chairman, as far as the refunds that are received by Colorado utilities and Wyoming utilities, there is a requirement that all of the refunds, except maybe for some out-of-pocket expenses related to acquiring those refunds are going to be dollar for dollar refunded to customers.

Now, there may be situations—as Ms. Stovall suggests, there are some private contract matters between the interstate pipelines and direct sales customers, which it could be that the direct sales customer provided that it will receive the refunds depending on the pricing provisions of those private contracts, but that is not an NGPA- or NGA-regulated sale.

Mr. SHIMKUS. As far as I understand this issue, refunds have been given back from 1988 on; is that correct?

This issue is from 1983 to about 1988 that we are dealing with. What has been the process of the refunds from 1988 to what was

it, 1993? Anyone want to speak to the process of the refunds? Mr. Albright, you look like you are interested in—

Mr. ALBRIGHT. The process is virtually the same as adopted for purposes of these refunds which is that the pipelines submit a report to the FERC that gives a list of the providers, the producers, the suppliers that provided the gas during this period of time and its calculation of what the refunds are that are due from those producers. They also sent notices to those producers directly pursuant to the rule that perhaps Mr. Smith can discuss a little bit more elaborately.

Mr. SHIMKUS. I wanted to ask Mr. Smith if Ms. Stovall is correct. How would you respond?

Mr. SMITH. A couple of points.

First, the Commission's order in 1997 provided that the refunds need to be flowed through by the pipelines. In considering requests for clarification of that order, the Commission permitted three pipelines that have by far the smallest refund amounts due, to retain the refunds. They had settlements with their customers that allowed the pipelines as opposed to the pipeline customers to retain any refunds that might be ordered.

There are nine pipelines that are affected by the refunds. Those three account for, I think, 1.5 percent of the total amount of refunds, so they are by far the smallest on the list.

The second issue is the flow through by the local distribution company. The pipelines are required, with that exception I noted to flow through the refund amounts to the local distribution companies. The issue, as had been mentioned earlier, of whether the local distribution companies flow those refund amounts through to their end-use customers is a matter of State regulation.

And as Mr. Albright mentioned, at least in some States and maybe in all States that are affected, the State commissions have been careful in reviewing how that works and are trying to get the refund dollars through to end-use customers. The mechanics of how that is happening may vary from State to State.

Mr. SHIMKUS. Who determines how much is owed by each individual producer or royalty owner? Who is making that final determination? When someone opens up the mail, surprise you owe \$25,000; who is making that decision?

Ms. STOVALL. Right now it has been made by the pipeline companies. They have simply been ordered by FERC to come up with a bill, and that is what they did. They did it by November of last year and in 6 months then the royalty owners and the gas producers had to have that amount put in escrow by March of this year.

So there has been no determination. It is simply the pipelines sending a bill and there has been no process yet to have a due process hearing to contest those amounts because one of the keys is that refunds are only owed if the companies paid more than the maximum lawful price. Our understanding is from what we have looked at, the bills are being submitted assuming maximum lawful price was paid plus the tax, and that has not been the case when we have had an opportunity to look at the records.

Mr. SHIMKUS. Mr. Smith, I am going to follow up on some other issues on the hardship issue. Talk to me about this—the determination of the amounts.

Mr. SMITH. The Commission's orders require the pipelines to serve a notice on the producers that sold to them of the pipelines' calculation of how much refund is due. The process for resolving any disputes between the producer and the pipeline is that the producers file with FERC a request for adjustment that essentially says the pipeline gave us notice that we owe X dollars and we think we owe Y dollars. Then there is a process at FERC for resolving that issue.

Mr. SHIMKUS. Ms. Stovall, do you agree there is a process for resolving the conflicts between the bill and what—the person who is being charged this amount?

Ms. STOVALL. Not to date.

Mr. SHIMKUS. I think our colleague Congressman Moran made the statement that there was no due process.

Ms. STOVALL. There has been no due process. FERC seems very reluctant to grant those hearings to the producers. It is my understanding producers have indeed asked for that and there is no indication that FERC is eager to take this on because it is thousands of people coming forward to contest these bills.

It would be a nightmare for them to do, but they need to. The key is even though there hasn't been this process, they have been ordered to pay 100 percent of the money without any judicial determination.

Mr. SHIMKUS. Let me bounce back to Mr. Smith then. I know you have addressed hardship cases. I still want to eventually ask that, but have you addressed any dispute resolutions between the person who has been billed and those who want to question the amount? They are separate, and I want to make sure we keep those separate.

Mr. SMITH. I don't think we have come to a final resolution on any of those issues.

Mr. SHIMKUS. What does that mean? Have you had a hearing on a dispute resolution mechanism or not other than a hardship?

Mr. SMITH. We have not set any of the petitions for adjustment, which is the label we give to these disputes about how much is owed, for an adjudicative hearing.

Mr. SHIMKUS. Are we going to?

Mr. SMITH. That is a decision to be made by the Commission.

Mr. SHIMKUS. But in your testimony—just minutes ago, didn't you say there was a process to do this?

Mr. SMITH. There is a process, but it doesn't necessarily involve an adjudicative hearing.

Mr. SHIMKUS. Well, what does it entail then? That is right; I am having some success here.

Ms. Stovall, just hold off.

You are lucky that the ranking member is not here because you would be smoking by now. I am much nicer than he is.

Mr. SMITH. As I understand it, some producers have asked for a formal adjudicative hearing on their adjustment claims. As far as I know, there aren't any issues about particular disputes between particular producers and particular pipelines about refund amount owed for which the Commission has yet ordered such a hearing.

Mr. SHIMKUS. Well, let me move on. Because we would like to get that answer maybe in writing somehow.

Mr. SMITH. We can provide that answer.

Mr. SHIMKUS. Why I am following this line of questioning, as I mentioned in maybe my opening statement that the Federal agencies are supposed to be—we should serve our clients. Our clients are the consumers, and we need to make every effort to help them resolve conflicts prior to going to the court.

It is not just the FERC. This is the first time I heard of FERC not responding rapidly. I have other problems with other Federal agencies. So it is a good line of questioning. And those of us who want government to work well and work with the clients—I mean, I think all they are asking for is due process, a chance to question the bill, which I think they should have.

And I got a small producer here. Do you want to add anything?

Mr. KREHBIEL. Perhaps I can shed a little bit of light on that question.

The example that I gave in my testimony of the widow in Wichita, Kansas, she received a bill, letter from the FERC directing her to refund \$20,000. When I went back through what information was available when I tried to help her, I learned that she was actually underpaid by \$49,000 during the period from 1983 to 1988, and she is being held responsible for \$20,000 in a refund. She simply wrote back and said she didn't owe it.

So then we don't know what happens next. We got producers all across the State of Kansas who are being asked to pay refunds without any determination that they are even liable for the refunds. That is the really bizarre thing about this procedure. How can you ask a producer to refund \$20,000 based upon an alleged overpayment that is just based upon a conclusion presented to the FERC by the pipeline company? We have got records here that are 15 years old. You have got to go back and study a whole lot of issues and dig out a whole lot of records to figure out whether any liability even exists, and to my knowledge none of this has ever even been done.

Mr. SHIMKUS. Let me ask, since she hasn't been harassed that much, Miss Lumpe from Missouri, sister State to Illinois. In fact, some of the pipelines that go through Missouri end up in Illinois. What do you think about the claims of the small producers, chance that the FERC ought to at least hear the case and do some adjudicative process which makes some validity of their claims?

Ms. LUMPE. As I said, we are not unsympathetic to various hardship cases.

Mr. SHIMKUS. This isn't just hardship. This is questioning the billing, questioning the methodology, and coming to a conclusion. I mean, this is—I didn't go down the hardship case route. This is, are these bills certifiable? Are they—you know, are they supportable with documents and should there be a process by which the individuals who are claiming that they are now being harmed by this ruling, that they have their day in court?

Ms. LUMPE. My understanding is—and, again, I could be wrong, but my understanding is that there are procedures set up in the act that determine how—

Mr. SHIMKUS. Yeah, but you have been following our discussions of the past 5 minutes. And there may be procedures, but they are not—

Ms. LUMPE. Well, but they should be followed.

Mr. SHIMKUS. Thank you very much.

Ms. LUMPE. They should be followed.

Mr. SHIMKUS. Thank you.

Anyone else want to comment? Miss Stovall.

Ms. STOVALL. To file the petition for alternate dispute resolution, which some of the producers indeed have done as far as back as March and not had response from FERC, costs \$13,000 per pipeline to do that. For small producers, that is a huge bit to ask them to resolve what they lawfully owe.

Mr. SHIMKUS. Mr. Majeroni.

Mr. MAJERONI. If you think about the royalty owners' point of view, unless you are really from Kansas, I mean, your local attorney, your family attorney knows nothing about any of this. And who do they turn to for help? You know, the cost of getting that help is almost, you know, as much as the bill. So it is a real problem. And——

Mr. SHIMKUS. Well, again——

Mr. MAJERONI. [continuing] 15-year-old bill to try to find those and verify those.

Mr. SHIMKUS. Again, we have done the same thing in a landfill in Quincy, Illinois; and the consumers at least got an opportunity to go back and pull out their own dumping records and have at least a small portion of their day in court. And I think that would probably make the individual parties at least somewhat understandable of the process if they at least had a chance to fight this charge.

With that, I am going to yield back my time to the chairman.

Mr. BARTON. Recognize the gentleman from Oklahoma for 10 minutes.

Mr. SHIMKUS. Do I have to? I mean, yes, I would like to recognize the distinguished gentleman from the State of Oklahoma for 10 minutes.

Mr. LARGENT. Thank you, Mr. Chairman.

Ms. Stovall, I want to get down to the basics a little bit. Tell me about what is an ad valorem tax in this context? I mean, what are we taxing?

Ms. STOVALL. In Kansas, the way the tax has been put on is a complex formula. I am not going to pretend that I have an in-depth understanding of it, but it taxes various things including the rate of production as well as other factors. And there is a property valuation done as to what the reserves are worth. There is a calculation taken based on how much production is taken from the natural gas well each year which is how those prior decisions were made saying that it is a production tax.

Mr. LARGENT. Okay.

Mr. BARTON. Would the gentleman yield on that?

Mr. LARGENT. Yes.

Mr. BARTON. But the tax that was paid was paid on natural gas that was actually produced from the well in a given month, is that not correct? They didn't tax at the end of the year based on the value of the reserves still on the ground. They taxed on the amount of natural gas that actually came out of the well.



Ms. STOVALL. The amount that came out of the well was one of the factors in calculation of the tax.

Mr. BARTON. Only one of the factors.

Ms. STOVALL. Yes, sir.

Mr. BARTON. So they did have a kind of a reserve tax also.

Ms. STOVALL. That is why it was an ad valorem tax.

Mr. BARTON. I didn't know that. That is different.

Ms. STOVALL. It was a little bit different than the ones—

Mr. LARGENT. Can you enlighten us on that at all?

Mr. KREHBIEL. Perhaps I can. Ad valorem tax was based on the amount of the production and the value of that production, but there is a reserve analysis, as you suggest. So it was a combination of factors.

And the law at the time said severance production or other similar taxes, and in the FPC ruling they ruled this was a similar tax. It was based upon production. You report the amount of your production every year, and you report the value of that production, the price that you got for the production. So you have those production and price factors figured into it. And that is where they come up with the idea that it was a similar tax.

Now if the State of Kansas had known that they were going to change their mind on how this was—

Mr. LARGENT. We got that part of the argument.

Mr. Albright, based upon that, the ad valorem tax, it sounds like it is a fairly complicated issue that deals with production and reserves, calculation, like that. You were—what was the quote that you had that the Circuit Court had on whether the ad valorem tax could be, basically, passed on to the ratepayers?

Mr. ALBRIGHT. According to the D.C. Circuit—let me pull that exact quote: "We are hard pressed to see how the producers would be harmed in any cognizable way even if they were required to disgorge every dollar they received in recovery of the tax."

Mr. LARGENT. But I am talking about in terms of what the Circuit Court said to FERC about their allowing Kansas to pass on to ratepayer the tax instead of going to the producers.

Mr. ALBRIGHT. I didn't quote that, but that is the CIG case in 1988 where the Court examined the analysis that FERC had applied, in comparison to the Texas tax, the same analysis against the Kansas tax. And in the Court's mind this was a dissimilar treatment of what the Court viewed to be similar taxes and called the Commission's actions the quintessence of arbitrariness and caprice and remanded the case back to the Commission to exercise its interpretive authority to identify the features of the Kansas tax that point toward one classification or another and to offer sensible distinctions between taxes that it chooses to treat differently.

So there is a Commission decision which came out in 1993, and that is Colorado Interstate Gas Company, 65 FERC, paragraph 61, 292, that the Commission issued which examine in length the features of the Kansas tax supporting the determination that it was not a severance tax but, in fact, a tax on property.

Mr. LARGENT. Okay. It sounds like it is much more complicated than the conclusion reached by the Circuit Court. That is my point. To me, when I hear the explanation of the tax, it is not a real simple value-added tax that doesn't have anything to do with produc-

tion, it has a lot to do with production. So I don't know that it is a clear-cut case that this cannot or at that time could not be passed on to the ratepayers.

But I want to go back to Mr. Smith. Mr. Smith, in 1988 FERC was given this decision and remanded the case in 1988. It took FERC 5 years to make a decision. Why the delay? In getting such compelling language from the Circuit Court in DC, remanded the case to FERC and said, you guys need to do something about this, and there is a 5 year hold-your-breath. What happened?

Mr. SMITH. Well, I wasn't at FERC at the time, so I can't speak from personal knowledge, but, as you can hear from today's hearings, these are difficult issues with strongly held views on both sides, and it took that long to get an order out of the Commission.

Mr. LARGENT. How many cases have there been where people have been ordered to pay and they have sought, you know, some reprieve from FERC?

Mr. SMITH. The special hardship?

Mr. LARGENT. Yeah, how many cases.

Mr. SMITH. I think we have got roughly 130 applications already.

Mr. LARGENT. How many have you actually heard?

Mr. SMITH. Well, we have acted on 10 roughly, 10 or 11.

Mr. LARGENT. And, Miss Lumpe, how many has Missouri appealed?

Mr. BARTON. Again, use the microphone for our recording clerk.

Ms. LUMPE. Missouri has appealed a number of them. Somewhere I have the precise number.

But what we have really done is say, have they given you adequate data and information? We haven't said that they were wrong. We said we think that the FERC should have adequate documentation and data that these are truly hardship cases. And if they are, we would not contest them further. We simply think that they ought to have adequate information to make their determination.

Mr. LARGENT. Okay. Mr. Smith, in somebody's testimony here it said that \$95 million has already been paid. Where is that money?

Mr. SMITH. It has been passed from the producers to the pay plans, through the pay plans to the LDCs.

Mr. LARGENT. LDCs?

Mr. SMITH. Local distribution companies. To the customers of the pipelines.

Mr. LARGENT. So it actually has gotten to the consumers?

Mr. SMITH. Well, the other witnesses can comment on what happened to it, at least in a few particular States, after it got to the local distribution companies.

Mr. LARGENT. Miss Stovall.

Ms. STOVALL. It was my understanding the money is held in escrow. Certainly the \$21 million paid into Kansas has been held in escrow pending resolution of who owes what and validity of the claims.

Mr. LARGENT. Miss Lumpe.

Ms. LUMPE. The money in Missouri coming from the pipeline to the local distribution company and through our purchase gas agreement factor that we used flows directly then to the consumer.

Mr. LARGENT. So there is checks already been handed to consumers.

Ms. LUMPE. I am not aware of any of that. That would be the process would occur should the refunds and interest come to us.

Mr. LARGENT. But you have gotten some refunds, is that right, of this \$95 million? Hasn't some of it come to the State of Missouri?

Ms. LUMPE. I am not aware of that number, sir.

Mr. LARGENT. You are not aware of it?

Ms. LUMPE. I am not aware that we have passed to LDCs in Missouri.

Mr. ALBRIGHT. If I may speak. The Public Service Company of Colorado received a refund of over \$2.5 million, and almost all of that has been refunded to its customers by now.

Mr. LARGENT. And that has gone to individual ratepayers.

Mr. ALBRIGHT. Yes, it has been credited to the bills of the customers.

Mr. LARGENT. Did any of it go to pipeline?

Mr. ALBRIGHT. None. Some of it went to the Colorado Energy Assistance Fund, which is a low-income fund for consumers.

Mr. LARGENT. Was it ever held in escrow?

Mr. ALBRIGHT. None of it was held in escrow by public service. I think Miss Stovall is referring to the fact that some of the producers have the option of placing the funds in escrow until the litigation is resolved.

Mr. LARGENT. But not in the State of Colorado.

Mr. ALBRIGHT. Well, that is a FERC matter. That is a Federal matter. I believe Mobil Oil Corporation actually did pay some \$62 million, in that ballpark, of refunds, which is the bulk of the \$90 million that Mr. Smith is referring to.

Mr. LARGENT. Miss Lumpe, do you have some new information?

Ms. LUMPE. Yes. About \$8, \$9 million has been sent back to Missouri and through the MGE, the local distribution company known as Missouri Gas Energy.

Mr. LARGENT. What they have done with it?

Ms. LUMPE. Then they come to us and through a credit we refund it back to the consumers.

Mr. LARGENT. One hundred percent.

Ms. LUMPE. One hundred percent.

Mr. LARGENT. So the money was not held in escrow in Missouri either.

Ms. LUMPE. I don't believe so.

Mr. LARGENT. I wanted to kind of walk through there—I mean, the reason I ask that is because I want to talk through—in the Chairman's remarks he said that the pipelines paid the tax. Is that true? The pipelines paid this tax? Or did the ratepayer pay the tax? Miss Stovall.

Ms. STOVALL. Certainly, ultimately, it would have been the ratepayer.

Mr. LARGENT. Because the pipeline just passed it right on to the ratepayers.

Mr. BARTON. I mean, when they paid the purchase price they included the maximum lawful ceiling price and it also included Kansas taxes. So the pipeline paid it, and the distribution company paid it. Then they added to the price that the ultimate consumer of the gas paid.

Ms. STOVALL. True.

Mr. LARGENT. It was passed along.  
Well, my time has expired, but I want to ask more questions later.

Mr. BARTON. The gentleman from Texas.

Mr. HALL. I have asked all I need to ask.

Mr. BARTON. The Chair—

Mr. HALL. I have my mind made up.

Mr. BARTON. We have some additional questions. But what we are going to do, now that everybody has had a 10-minute round, we will just have a general question period. And I will ask some questions, and if Mr. Largent and Mr. Shimkus and Mr. Hall—Mr. Shadegg indicated—oh, he is here.

The Chair would recognize Mr. Shadegg. We are not used to him sitting with the staff in the back of the hearing room. The gentleman from Arizona is recognized for 10 minutes. Mr. Shadegg.

Mr. SHADEGG. Thank you, Mr. Chairman. I will be brief. I won't take my full 10 minutes and may be able to pass some on to you.

Do I understand from the Attorney General of Kansas that, having listened now to the other people in the room, that Kansas is apparently the only State that is, in fact, holding some of these moneys in escrow at this point?

Ms. STOVALL. Oh, I am not at all sure that is true. There are many, many States involved. The two here apparently aren't holding in escrow, but there are lots of States who have consumers who may get that \$10 of refund if indeed it is paid. So their individual corporation commissions have to rule on what happens with that money, and it hasn't happened in many of the States.

Mr. SHADEGG. But your position as the Attorney General of Kansas is it would be better to follow legislation such as Congressman Moran has introduced and pass this back onto the pipelines, as opposed to trying to carry it to the individual consumers.

Ms. STOVALL. Congressman Moran's bill would say the only way that the producers have to pay this rebate is if it goes to the ultimate consumer. And that guarantee we would want. If anything is to be done, it has got to go ultimately to the consumer, not to the pipelines.

The moneys that we have talked about earlier by Mr. Albright, the hundred percent of the money went to the consumers, it is my understanding that the money from the pipeline—that the pipelines kept was taken off the top of that. So, indeed, what he said was true. One hundred percent of the money that he spoke of went to the consumers, but that was after an element of the money was kept from the pipeline companies.

Northern Natural Gas intends, it is our understanding, to keep 20 percent of it, Panhandle Eastern to keep 11 percent, and so on. That comes off of the top. So that needs to be clarified and how much the consumers ultimately may get.

Mr. SHADEGG. Do you agree with that interpretation, Mr. Albright?

Mr. ALBRIGHT. I don't know if I agree with those figures. Colorado's primary interstate supplier is Colorado Interstate Gas Company, and they have indicated that they are only going to retain about 5 percent of the total refunds. This is a result of direct sales,

not sales for resale which is regulated by FERC. The direct sales are not regulated by FERC but subject to State regulation.

So if there is a matter of State regulation involved, I am not sure how that is being passed on in other States. With respect to Colorado, it is not regulated. It is a matter of private contact law.

So it depends on the bargain that was struck by the direct user, the end user of the gas, and the pipeline. It could be that the direct end user will receive that refund pursuant to the terms of the contract. Otherwise, the pipeline would retain it because they get the benefit of the bargain.

Mr. SHADEGG. Let's go back to the issue of the interest. The largest portion of this, some \$25 million of the \$363 million is interest. However, under Mr. Moran's legislation, that interest would be waived and the refunds. That would simply be limited to the principal amount originally taken. Is that correct?

Ms. STOVALL. That is correct.

Mr. SHADEGG. Your view is that is a necessary step for the viability of the gas industry in Kansas?

Ms. STOVALL. That is true, as the equity would require that in recognition of the delay and reliance on FERC decisions and the rest of it, absolutely.

Mr. SHADEGG. Does FERC have a further explanation? I know Mr. Largent asked a little bit about it as to why it did take from a period of 5 years to try to decide this issue. I mean, I understand it is complicated, but it seems to me the Court language was fairly clear.

Do you know of any further explanation FERC has for this? And, given the delay, why would FERC then at least not be supportive of the aspect of Mr. Moran's decision which waives interest—Mr. Moran's legislation which waives interest?

Mr. SMITH. I don't have any further explanation of why it took 5 years for the FERC to issue the remand order.

On the issue of what the Commission did in response to the second D.C. Circuit decision, it concluded that a generic waiver of interest wasn't consistent with the reasoning of the D.C. Circuit in its 1996 decision.

The rationale for not taking a position on the current legislation is that the Commission, in this respect views its job as administering the current statutes interpreted by the Commission and by the Courts. And if the Congress comes to a different judgment about what the equities require in terms of how to share the liabilities, that is a congressional prerogative and the Commission will do its best to administer the law however it might be amended.

Mr. SHADEGG. I guess, too, that last point—I certainly agree it is your job to administer the laws as we enact them. Are you an attorney?

Mr. SMITH. Yes.

Mr. BARTON. No, he is just the General Counsel at the FERC.

Mr. SMITH. It is buried in my job description someplace.

Mr. SHADEGG. It is good to know that the FERC has an attorney for their general counsel. I am pleased to hear that, Mr. Chairman.

But in that regard I want to ask you a question that Mr. Albright raised. You do not see a change by the Congress at this

point in time of the status of any interest as being unconstitutional, do you?

Mr. SMITH. I know the issue has been raised but, it has not been raised with the Commission. So the Commission hasn't come to a judgment about that. I would note that the Commission does have authority under existing law, section 502 of the NGPA, to provide for waiver relief, and I am not aware that anybody has questioned that authority as being unconstitutional.

Mr. BARTON. Would the gentleman yield on that?

Mr. SHADEGG. Certainly.

Mr. BARTON. What authority does the FERC have, since this is a State tax that was levied, to assess penalties and interest on a tax? I thought the Constitution gave the Congress the right to assess taxes.

Mr. SMITH. The relationship between the producer and the State in terms of the tax payment was not something that the NGPA envisioned the Commission having any role in. As you are aware, the issue in this case is essentially one of rate regulation under the NGPA and whether the tax payment can or cannot be passed on from first seller to the pipeline.

Mr. BARTON. I understand that. But my question is, if the gentleman will continue to yield, and I don't know the answer. Sometimes I ask questions to set people up because I think I know the answer. But this time I am actually asking because I actually don't know and, hopefully, you do.

Where does a Federal agency have the right, since this is a State tax—I understand that FERC has the right to regulate prices of natural gas because the Congress gave the Federal Power Commission that right under a prior act to the NGPA, but where do you have the right to establish an interest in what I would call a pen leak because it is a State tax? Why wouldn't you just say refund the principal as the Moran bill does? Where do we get the authority to go above and beyond that—not you personally but the Commission.

Mr. SMITH. I think the authority is in the NGPA itself, which provides the generic authority to set the rates, and in the traditional exercise in rate making of applying interest to refund calculations.

Mr. SHADEGG. Reclaiming my time, if I might, perhaps I can answer the gentleman's question.

I think the answer is that, as a regulatory agency charged with setting the price, if a price is collected above the legal maximum, a penalty can be imposed saying you charged a price above what was allowed. And so you are going to have to give that back, and you will have to give back interest on that. And I don't know that. But—

Mr. BARTON. But they never questioned the rate. There is no dispute—

Mr. SHADEGG. But it was included.

Mr. BARTON. [continuing] the maximum lawful ceiling price. And Kansas never hid the tax. Kansas never said, this isn't really a tax. They were always up above board. The people that purchased the gas knew that it was a tax.

Mr. SHADEGG. We established that neither counsel nor I know where they get the right to charge the interest.

Mr. BARTON. I don't either.

Mr. SHADEGG. And neither do you. But I would like to go back to this point of constitutionality, because it is well established in tax law in this country and has been for a very, very long time that you can enact retroactive taxes. And indeed I believe in North Dakota at one point in time the State went back and enacted a retroactive tax that went back a period of 8, 10, 12, 15 years. They collected the tax, and it was challenged, and it was upheld as being a lawful act of the State legislature.

In that instance, I think what happened was the legislature thought they had enacted the tax, they discovered that they had not properly enacted the tax, and they went back years later and reenacted the tax and that was upheld.

So I don't think that were this Congress to pass Mr. Moran's legislation giving back this interest at this late point in time that that would be unconstitutional, nor do I think it was a taking. I think it would be perfectly lawful under our law and indeed maybe demanded by the equities.

I guess the other point I want to make was in response to Miss McCarthy's point and that was I do not see any problem with this Congress reversing a decision of a court. That is a part of the co-equal branches of government. If we believe a court has made an ill-advised decision, I think we are in a position to and often do reverse court decisions. And I think, at least in the State of Arizona where I am from, the legislature frequently looked at court decisions with which it disagreed and reversed those court decisions where the legislature felt equity demanded it.

I will yield back what little of my time.

Mr. BARTON. Well, I took some of the gentleman's time. So did you have another question?

Mr. SHADEGG. No, I am fine.

Mr. BARTON. Well, I have a few wrap-up questions.

I want to thank the panel. You all have been here since 10, and you have been testifying since about 10:45. And so, hopefully, in the next 10 minutes we can conclude. And I know Mr. Largent has some questions, too; and Mr. Shimkus does.

So my first question and, again, I will just recognize people as they have questions instead of giving us each an X amount of minutes.

Miss Lumpe, I heard you in your oral statement and again in reply to a question that the great State of Missouri is not interested in trying to go after the widows and the orphans, so to speak, that your interest is in getting what is rightfully due to the State in terms of those big old bad producers that have all that money. But Senator Roberts sent over some case histories for me to put into the record; and I am just going to ask you about them because, if nothing else comes out of this hearing, perhaps we can use your good offices to get some justice.

The first case that Senator Roberts sent over is a Mrs. Merland—I want to say Cope, C-o-p-e, Calvin of Arizona. Her husband's health has failed—and I believe that her husband has passed away. She owes \$9,000 in refunds. She hired an attorney,

went to the FERC. The FERC gave her a hardship waiver after 7 months of consideration, and the Missouri Public Service Commission has appealed that. Are you aware of that particular case?

Ms. LUMPE. I am not aware of the particular one, but I do know that we have appealed a number of them. And the reason we have is because we are not aware that the FERC got adequate data or information to make that determination. That is the process that we are asking for in our request.

Mr. BARTON. I am not going to read the inflammatory sentence that Senator Roberts put in. But I am going to ask that you look at court case number 99-1103. And, again, if these documents are correct, this elderly lady only owes \$9,000; and the FERC did grant her a hardship waiver. And the Missouri Public Service Commission, according to Senator Robert's office, is appealing that.

The second case is a Mrs. Bone of Colorado, and her mother passed away. So she inherited some royalties from her mother. She was asked to pay \$12,998. She appealed for a hardship waiver, and the FERC again granted the hardship waiver, and the Missouri Public Service Commission again is appealing that. Are you aware of that case?

Ms. LUMPE. I am not aware, again, of the specific case. The cases that we have appealed have been based on the process that we felt that a letter being sent and just asking was not sufficient, that there should be some evidence of hardship.

Mr. BARTON. All right. Well, if you will look up the case of Bone of Colorado.

And there is one more. This is a Mr. Freeman, who is still alive. In this case, the person who actually had the royalties is alive. But he has heart disease. He is 64 years old. He owes, according to the documents, approximately \$100,000. The wells are no longer producing. His only income now is social security, and he applied to the FERC for a hardship waiver. Actually, Mr. Freeman's partner, a Mr. Lee Kizner, who is dead, was the one that was supposed to pay this \$100,000.

And it doesn't say that the FERC has actually given a hardship waiver here, but that the Missouri Public Service Commission has already intervened and protested Mr. Freeman's request to waive the refund obligation. And they want to know—and this is again according to Senator Roberts—they want proof that the royalty owner is actually dead. They want information demonstrating that he, Mr. Freeman, attempted to collect the refund from the dead royalty owner, including lodging a claim for the refund with the deceased's estate, and they want proof or documentation that making such a refund payment would cause special hardship. So could you check that one, too?

Ms. LUMPE. Certainly.

Mr. BARTON. Okay.

Mr. HALL. And their boy is in jail, isn't he?

Mr. BARTON. And I will provide—

Ms. LUMPE. Mr. Chairman, do you have the numbers?

Mr. BARTON. Yes, ma'am.

Ms. LUMPE. You gave me the numbers of the one case, but not the other two.



Mr. BARTON. I will give you all the documentation that Senator Roberts gave me. You seem to be a very honest and decent woman, and if you will go back and check these out. If they turn out to be as they are stated on the record, at least we could get some justice for these three.

Ms. LUMPE. Right. And, as I said, we are not unsympathetic to them. We just felt there should be the process and the documentation before it is automatically granted.

Mr. BARTON. My last question before I yield to Mr. Shimkus or Mr. Largent, Mr. Krehbiel, you indicated in your answer to Mr. Largent that the calculation of this tax was based on a reserve, a reserve calculation as well as a production calculation. What would be the case if there was a well that has not produced but had an established reserve? Would they pay a tax in that calendar year even if there was no production from the well?

Mr. KREHBIEL. They would pay—I am not an expert in the ad valorem tax in Kansas as well, but they would pay a tax probably on machinery and equipment.

Mr. BARTON. I am talking about the value of the gas in the reservoir. Would they pay on the expected value—again, under the NGPA, you had a long-term contract, and you had a maximum lawful ceiling price. This was old gas, so if they knew how many mcf or billion mcf were in that well they would know the value of the reservoir because they had a ceiling price. Would they pay a tax?

Mr. KREHBIEL. I think there was an element of valuation based upon reserves in place.

Mr. BARTON. It is possible you could pay it—it is theoretically possible then—

Mr. KREHBIEL. I think the answer to your question is yes, theoretically.

Mr. BARTON. I started to say somebody would have never produced gas and then still be liable for this, but if they never produced they would have never sold it, so there wouldn't be a plaintiff out there wanting to be reimbursed.

Mr. KREHBIEL. Yeah. That is a very unique issue. Theoretically, yes.

Mr. BARTON. The gentleman from Oklahoma, Mr. Largent.

Mr. LARGENT. Thank you, Mr. Chairman.

Mr. Smith, what authority is there that oversees this process? I mean, does FERC take authority? Who is sending out a letter notifying a producer that you owe money? Who does that?

Mr. SMITH. The pipelines have filed reports with us saying what they believe the refund obligations are.

Mr. LARGENT. So then a letter comes from FERC to one of these producers? Santa Fe Minerals would get a letter from FERC saying you owe us.

Mr. SMITH. They got both a notification from the pipeline which had that producer on their list of people that owed refunds, and they got a letter from the staff at the Commission.

Mr. LARGENT. Okay. And they are ordered to pay X amount of dollars to whom?

Mr. SMITH. The refunds are to be paid to the pipeline.

Mr. LARGENT. To the pipeline.

Mr. SMITH. Yes.

Mr. LARGENT. And then who tells the pipeline what to do with this money?

Mr. SMITH. We have told the pipeline what to do with it. They need to pass it on to their customers, with the exception of the three pipelines I noted before that have settlements with their customers that allow the pipelines to retain any refund amounts.

Mr. BARTON. Would the gentleman yield on that point?

Mr. LARGENT. Yes.

Mr. BARTON. What documentation did the FERC require of the pipelines to prove the value of the refunds being requested?

Mr. SMITH. My staff is helping me.

Mr. BARTON. We appreciate that you have a staff that wants to help. Hopefully, they actually can help.

Mr. SMITH. I am especially appreciative.

The initial filing by the pipeline simply listed the producers and the pipelines' estimate of the refund liability for each producer. The Commission's letter to the producers that was based on that list said that if the producer disputes the amount that the pipeline has as the refund calculation, then they should, in the first instance, see if they can work it out with the pipeline, but, if they can't, then raise their disputes with the Commission.

Mr. BARTON. But there is no requirement that the pipeline or the requester of the refund document the amount before the fact.

Mr. SMITH. Right. Only in the case when there is a dispute presented to the Commission about the refund amount would we get into who has got what evidence of that amount.

Mr. LARGENT. Is there documentation that the pipeline company is responsible to produce for FERC in terms of the distribution of those moneys?

Mr. SMITH. Yes, they file something with the Commission called pipeline refund reports.

Mr. LARGENT. And what happens to any money that is not distributed? In other words, they can't find the ratepayer. Where does that money go?

Mr. SMITH. I don't think that issue has been raised with the Commission yet.

Mr. BARTON. Could we have the name of the lady in the purple who seems to be answering most of these questions? Just for the record I think we ought to—

Mr. SMITH. Give her credit.

Mr. BARTON. What is her name and title?

Mr. SMITH. Marilyn Rand.

Mr. BARTON. You are the Director for the Division of Pipeline Certificates.

Ms. RAND. Yes.

Mr. LARGENT. We are glad you are here.

Okay. So we don't know what happens to any excess money? I mean, would producers earn interest on that money that is being held by the pipelines that could be credited? I mean, it has got to go both ways, doesn't it?

Mr. SMITH. I am sorry?

Mr. LARGENT. They pay in money. It is not being distributed to the ratepayer, who we are so concerned about. It is being held in

escrow, in essence. Why can't they get interest credited for that money?

Mr. SMITH. If the pipeline holds the refund amount that they receive from the producer for more than 30 days, then the pipeline is liable for interest to its customers.

Mr. LARGENT. We are really getting complicated here. I have one other question, and that is to Mr. Albright.

Mr. Albright, you said that when the State of Colorado got some of this refund back that they distributed some of it to who, \$2.5 million?

Mr. ALBRIGHT. It is called the Colorado Energy Assistance Fund, which is a statutorily created agency to administer to low-income consumers for energy.

Mr. LARGENT. Okay. Now, in your testimony in the summary it says it took 16 years for the customers of these producers to vindicate their right to the return of the excessive collections with interest using the legal process established by Congress in the NGPA. What right does the State of Colorado have to divert that money without the consumers' authority to a special slush fund for low income?

Mr. ALBRIGHT. I think there is somewhat of a misconception about which particular individual consumers will receive these refunds. The way the regulatory process works in the States—and I know of no exceptions—there is no way to identify individual customers from 1983 to 1988 that were specifically overcharged as a result of the Kansas ad valorem tax overcharging.

Mr. LARGENT. So what are we talking about? Where is the money going to go?

Mr. ALBRIGHT. It goes to the customer base of those utilities.

Mr. BARTON. Would the gentleman yield?

Mr. LARGENT. Yes.

Mr. BARTON. What if I could prove that I lived in Colorado from 1983 to 1988 and that I was a natural gas consumer and I even had records of what I paid to the Colorado Natural Gas Company that provided gas to my home? Could I petition for a refund with interest in penalties based on documents that I lived there for that time period, even though I have now moved to Texas and am living on a farm and become a hippie and are using solar power and don't want any hydrocarbon energy of any kind?

Mr. ALBRIGHT. Then you would probably be in Colorado.

Mr. BARTON. That may be true. I mean, what if I could actually prove with documents that I was one of these consumers that ended up paying the price that included the disputed taxes?

Mr. ALBRIGHT. Well, you would probably receive a refund from the current natural gas service provider where you live in Texas. You could petition to Colorado, but I believe the law would not be on your side because of the fact that the automatic adjustment mechanisms in the tariff provide notice of how refunds will be processed, how gas costs and upstream pipeline supplier costs are passed through to individual customers.

Mr. BARTON. Now, there is no dispute that the ultimate payer of the tax was the person or the industry that ultimately consumed the gas. The pipelines—again, at that time most of the pipelines

did take ownership. They actually paid the tax to the State of Kansas, as I understand it.

Mr. ALBRIGHT. I would take exception to that. Because Colorado Interstate Gas Company actually received gas bills from the producers from which it purchased gas and reimbursed the producers directly. It may have been different for other pipelines.

Mr. BARTON. I am not enough of a natural gas expert to know exactly how the billing was done. But, I mean, there is not a pipeline that is saying that the pipeline themselves paid the tax and didn't pass it on.

Mr. ALBRIGHT. That is correct. They did pass it on.

Mr. BARTON. They did pass it on. That being the case, if we were to move legislation in this subcommittee that is similar to the Moran bill, would pipelines take exception if we added an amendment that if you can't find the actual consumer who paid and purchased and consumed the gas any funds would go to some sort of a public benefit fund to be distributed to the State similar to what your line has apparently done in Colorado?

Mr. ALBRIGHT. Well, the way I understood Mr. Moran's bill was the reference to ultimate consumer would be the body of consumers that were customers of the utilities, the local distribution companies of the pipeline. So to the extent Public Service Company of Colorado is a customer of the pipeline, the bill would require that Colorado Interstate Gas Company, Williams Gas Pipelines, Cane Interstate Gas Transmission would make those refunds to the Public Service Company of Colorado.

What happens after that point, I think if the bill is to require that the actual consumer that received the bill that included some allocated costs of the Kansas ad valorem tax—and I would submit that that is an impossibility to do that because of the way rates are determined—but if that could be done, the cost of tracking each individual customer that was on our system—we have 1 million customers on our system—would outstrip the entire dollar amount of the refund.

We have 1 million customers on our system. And on an average monthly basis 20,000 of them move addresses. So to be able to track those customers that have moved from the service area would be a virtual impossibility. But the equities still weigh in favor of the consumers receiving these in refunds because consumers in Colorado may have moved to Texas.

Mr. BARTON. I understand that. But if you are going to have pure equity though, if you can't identify the consumer, if we are going to be fair about this, we ought to identify the consumer. And if we can't because we are a just society, instead of letting the pipelines, who admittedly never paid the tax, I mean, they got compensated, why not give to the public benefit funds of the State?

Mr. ALBRIGHT. Because then refunds would never be made to consumers for overcharged gas prices.

Mr. BARTON. But you just admitted it is—I think your exact words—it is virtually impossible to identify the consumer, the real consumer.

Mr. ALBRIGHT. It is physically possible to do, but the costs would just be enormous.

Mr. HALL. Mr. Chairman, would you yield?

Mr. BARTON. I am going to yield back to Mr. Largent, who can yield back to you.

Mr. HALL. When you talk about consumer, are you talking about the electric and gas customers?

Mr. ALBRIGHT. The natural gas customers, not electric.

Mr. HALL. Back to just the consumer in general, that would have to be a fund like the chairman suggested there—

Mr. ALBRIGHT. I am not sure what the chairman was suggesting.

Mr. HALL. [continuing] for my State to be part of those consumers, if we are just going to throw back someone that is not either a customer of the electric or the gas customer.

Mr. ALBRIGHT. Well, it is all done under State authority. The State regulatory Commissions provided for the pass-through of these costs, and they are regulating the refunds as well.

Mr. HALL. I will yield back my time.

Mr. LARGENT. I want to follow up, just kind of hammer at this point.

Mr. BARTON. I think we have Shimkus and Mr. Pickering.

Mr. LARGENT. I am going to take 60 seconds or less.

The point is that this action by FERC is really punitive. I mean, we are not trying to remedy a consumer, according to your testimony, because we can't identify that consumer—or customer. In fact, I would say that if we could put together a bill not like Jerry's but just say every person that can legitimately make their case that they were a consumer in the State of Colorado or Missouri or wherever during these years and you can validate that through your property taxes or State income tax that you paid or if you got your bills from 1983 to 1988, whatever, and can show those, we will pay you back, with interest. I bet that number would be significantly less than the number that is on this, you know, on this information that we have, \$366 million.

But that is not what this is about. This is about getting some extra money for consumers that were not necessarily harmed by this action in the State of Colorado.

Mr. ALBRIGHT. Except for the fact that they paid \$15 per natural gas bill too much.

Mr. LARGENT. Who did?

Mr. ALBRIGHT. The customers that were overcharged.

Mr. BARTON. If you can identify them, we will pay them. You just said you couldn't identify them. You said it costs more than it is worth to identify them.

Mr. ALBRIGHT. I think the expenses would be more than it is worth. I guess we are focusing on the relationship between the gas distribution companies and its consumers, whereas the matter here is between the pipelines and the customers of the pipelines that were actually overcharged. The way that the utility then refunds its customers, which in Colorado is 100 percent, is a matter of State regulation.

Mr. LARGENT. It is not 100 percent. You just said they put it into a low-income—

Mr. ALBRIGHT. But those are our customers. The low-income customers are still customers on our system. They just get a bigger share.

Mr. LARGENT. Well, it couldn't be 100 percent then. If you are putting some of it in a special fund, then you did not do 100 percent. There is no way.

Mr. ALBRIGHT. It is not a special—well—

Mr. BARTON. Mr. Pickering hasn't even had a chance to ask the first question yet.

Mr. Pickering, do you have questions? I know Mr. Shimkus still has a question.

Mr. PICKERING. Thank you, Mr. Chairman.

I appreciate you having this hearing. The longer I sit here—this is one of those examples that you just grow frustrated and outraged at the administrative, the regulatory, administrative and legal malfeasance and mal-administration and ridiculousness of trying to now rectify past wrong decisions over a 15-to-20-year period.

I speak of someone with great respect for the law and the courts. My father is a judge. But this is just beyond the pale to me of what we are trying to do, to the harm that it causes the independent producer, to the widow, to the student, to the sick. I mean, it is just, in my view, ridiculous.

Ms. Lumpe, how many widows are going to go through a traumatic experience? How many are near bankrupt or bankrupt? How many universities like Cornell will lose opportunities to educate for a perceived benefit of \$15 per consumer that you can never even find? You just said it is virtually impossible. Now where is the proportionality here of weighing the benefits to the cost?

And, Mr. Moran, I want to commend you for your effort here. I want to say that he has been diligent and persistent in calling every member on the committee. You could not find a greater champion to right what has, in my view, been just one of the cases that gives government and government confidence and integrity a bad name. So I am very thankful that we are having this hearing. I hope that we can move legislation through the committee.

You know, I could ask some questions, but I don't think I am going to find any more sense to this whole process than anybody else has found here.

Mr. Krehbiel, let me just ask you a few questions. And. Again, my home town of Laurel, Mississippi, is one where oil and gas and independent producers really contributed to our economy and to the founding as a major component of our community. So I have great sympathy of what you are dealing with and what the whole industry has been dealing with.

What will—if full refunds with interest are ordered, what impact will that decision have on drilling activity in Kansas?

Mr. KREHBIEL. The impact would be incredible. You are talking about enough money to fund the drilling budget for the entire State of Kansas for the next 3½ years. You will fundamentally cripple an industry that is already fundamentally crippled.

Mr. PICKERING. If Kansas producers had known in 1993 they couldn't keep reimbursements for Kansas ad valorem taxes, do you think they would have paid those reimbursements out to other working interest owners and royalty owners?

Mr. KREHBIEL. The oil and gas industry in Kansas has always complied with FERC regulations to the best of their knowledge and

ability. They wouldn't have done anything to not comply with Federal law. They wouldn't have distributed those revenues if they had any way of knowing.

Mr. PICKERING. Mr. Chairman, just one final question. How have the members of KIOGA been affected by FERC's answers dealing with the Kansas ad valorem tax issue?

Mr. KREHBIEL. We have got a lot of members totally in shock. They are just amazed that this can happen in this country. They can't project into the future. They can't set up drilling budgets. They have no idea where this thing is going to land. They are just sitting there waiting to see, waiting for the hammer to fall.

Mr. PICKERING. One final question for Ms. Lumpe.

You say that you want to process it as a case by case, that somebody has to demonstrate, provide demonstrable evidence of their hardship. Does that take retaining an attorney, a lawyer where you have tremendous legal costs in doing that? Can many of these people afford to do that?

Ms. LUMPE. I don't think it would take an attorney. I think what we saw was just a letter coming, saying could I have a hardship, and there was no evidence there. I think what we are asking is that there be some evidence.

Mr. PICKERING. But how do you collect and present evidence—take this widow in Kansas.

Ms. LUMPE. If the gentlemen said, my only income is social security and he has evidence of that, that is certainly enough. All widows are not poor. All people are not poor that are here. And we think that to get to the true hardship cases, you know, is what we are after. And so, because we are looking for the consumers of our State, I think that is our job and our mission.

Mr. PICKERING. The consumers that you could not find that are actually harmed.

Ms. LUMPE. They are a class of consumers that paid the unlawful rates over the—

Mr. PICKERING. Lawful at the time, though, is that not correct? It was a regulatory decision that was lawful at the time at least.

Mr. BARTON. Would the gentleman yield on that?

I think the gentlelady from Missouri is technically correct, but I would have to go back and look at it. But I am trying to remember what maximum lawful ceiling prices for old gas out of the Hugoton Field were in 1983. Gordon Gooch, in the back of the room, probably knows, but I will pull a number out of the air and say it was \$1 an mcf and then the severance tax and the ad valorem tax on top of that may have added 3 cents, maybe 4 cents. I don't know. Somewhere in that ball park.

The gas was consumed. The homes were heated. The turbines were turned. We are talking about even by the gentleman representing, you know, some of the larger plaintiffs in this, \$15 a customer over a period of years. There has been no harm done, nobody forced a gun to these people's head to consume and burn that natural gas. And the tax portion of it, unless Kansas is just a hugely high tax State, was almost negligible to the end consumer.

I yield back.

Mr. PICKERING. Mr. Chairman, I am finished as well and agree with your comments and views. And thank you for your leadership.

Mr. BARTON. Mr. Shimkus, do you want a final question?

Mr. SHIMKUS. Mr. Smith, on the—I mentioned when I was in the chair I wanted to quickly cite the hardship applications you have mentioned as the figures I have, that there are 130 requests and that I have 11 hardship applications that have been granted relief. Where are we on the additional 100 and will they see FERC responding in a timely manner to their requests?

Mr. SMITH. Let me just clarify the numbers. About 130 applications for hardship waiver have been filed. I think the Commission has acted on 11. We haven't granted all of them. My testimony stated how many were granted or denied or deemed unnecessary.

Mr. SHIMKUS. I am more concerned about the 119 additional.

Mr. SMITH. In most of those cases, there are two issues which need to get resolved before the Commission can act. One is simply getting enough information about the application for waiver so that we can make a judgment about whether there is or isn't hardship. At least some of the submissions we are treating as applications for hardship waivers are short letters that essentially just ask for the waiver without providing enough information to come to a judgment about whether there is or isn't hardship, and the Commission staff is trying to gather and check that information.

Second, in some of the cases, the waiver requests raised particular issues that are generic, and which are pending before the Commission. Some of these issues have recently been resolved at the Commission level. So that should permit us to move forward and act on the bulk of those pending applications.

Mr. SHIMKUS. And we, in essence, have been talking about \$334 million, and I have a list here that talks about, for example, what No. 1 is, Amoco Production Company, that has a principal owed of \$24 million and \$38 million in interest. Those interest rates keep accumulating; is that correct?

Mr. SMITH. Yes.

Mr. SHIMKUS. So if I have a chart that approximates from November 30th, 1997 to, well, just the end of December, 1997, obviously the interest rates are much higher now.

Mr. SMITH. I would note that some producers have paid. About \$95 million of the refund amounts have been paid. Obviously those aren't accruing interest. And some producers have paid refunds into escrow, so the escrow account itself is earning interest.

Mr. SHIMKUS. And the last confusion I still have is that the debate is on the ceiling set price when the natural gas industry was deregulated. And the dispute that we have also is whether at times from 1983 to 1988, was the actual additional charge to the Kansas ad valorem tax—did it actually go over the ceiling price? And there is still no reconciliation on that issue.

Mr. SMITH. One of the issues that has been raised before the Commission is referred to as the "head room" issue. It is basically the price that was actually charged below the maximum lawful price, so that even if you added—

Mr. SHIMKUS. It wouldn't matter.

Mr. SMITH. [continuing] the tax, it wouldn't matter, right.

Mr. SHIMKUS. I yield back to the chairman.

Mr. BARTON. Before I recognize Mr. Hall for concluding remarks, we are going to work to see if it is possible to get a consensus on



some version of the Moran bill and try to move it in the next month or month and a half.

Now, that may not be possible.

Mr. SHIMKUS. Mr. Chairman, can I interrupt as you are talking about that? It is a credible issue that has been raised too, and it has created sympathy for relieving the penalty and interest. And I know that is what my Congressman from Kansas wants. But it does set an interesting precedent. If we agree that there was an illegal tax, but it wasn't illegal enough to recoup the full benefits of money withheld, we put ourselves in an interesting position to say it was illegal enough to take the initial principal, but it is not illegal enough to also recover lost revenue over years.

Mr. BARTON. Well, the tax was not illegal. No one is saying that Kansas illegally levied a tax. The dispute is over whether the tax should be included in the maximum lawful ceiling price under the NGPA or whether it should be in addition to. And if it were in addition to, then it should have been borne by the producer, not by the consumer, not by the purchaser, because the NGPA didn't allow above the maximum lawful ceiling price. I think I am saying that right.

Mr. SHIMKUS. But is that bad enough to just ask for the principal back, or is it bad enough to ask for principal and interest.

Mr. BARTON. Well, we are going to see if we can make some people more happy and fewer people less happy than they are right now.

Mr. Hall, to conclude the hearing.

Mr. HALL. Mr. Chairman, I am back interested in it again. I am trying to figure who is stirring the pot.

Congressman Moran has absolutely touched all the bases. And he is not only a good guy; he is highly respected here. And you have given him his word that he is going to get a run. I don't know what the Senate is doing. You have read me some letters there from the Senator. You know, if each resident customer-consumer is receiving \$15, and each commercial resident consumer-customer is getting \$90, it is nothing to the utilities, it is a flow-through for them, as I see it; and the argument over interest is still in the Courts, and FERC is still litigating the generic waivers. And when you boil it all down it looks to me like the help to the customers doesn't seem like it is enough to justify the hurt it puts on the producers. And I don't think you are going to get lawyers to take any of these cases on a contingency basis.

I am trying to figure where we are coming from. I guess my question would be, who is the best constitutional lawyer there? Who is the best trial lawyer? Does anybody want to volunteer for that?

Mr. BARTON. Well, ask who is a lawyer.

Mr. HALL. Can I get this lady in purple to—

Counsel, why wouldn't the defense of de minimis be available to somebody here?

Ms. STOVALL. It certainly would in terms of the equity issue. We would argue very much, as you balance, that it is de minimis, the benefit that the consumers were to receive in light of the consequences, and that there isn't a constitutional right of the con-

sumers to interest, nor a constitutional right to the refund, but merely a statutory right to the refund.

Mr. HALL. Looks like everybody is in the same shape. The broke gambler, what he lost hurt him more than what he won helped him. I just don't see, other than courtesy to a good Member of Congress in giving him a hearing, where we are going with this.

Mr. BARTON. Would the gentleman yield?

Mr. HALL. Sure.

Mr. BARTON. Unfortunately, we had probably half the Republican members here; we only had, I believe, two Democrat members. But if we had had enough membership here to see what the consensus of the subcommittee—I want to move a version of the Moran bill.

Mr. HALL. You had the very best ones here.

Mr. BARTON. I didn't talk about the quality, I am talking about the quantity.

So if we can see that there is support for either the Moran bill or a bill similar to it, that it doesn't just absolutely cause heartburn to the great State of Missouri and the great State of Colorado and some of the other attorneys general and Governors that have sent letters on this issue, we will try to find equity and justice and move a bill that again is not identical to the Moran bill, but something that is similar to it.

I would say the chief addition would be the addition of a public benefits fund disbursement requirement, so that if you can't identify the consumer that actually paid the tax, that money would go to the State to use in some sort of low-income energy assistance or similar fashion.

Mr. HALL. I yield back my time. I thank the Chair.

Mr. BARTON. I want to thank this panel. There may be additional questions for the record.

We thank you for your attendance and thank the audience for their observation, and we are adjourned.

[Whereupon, at 1:18 p.m., the subcommittee was adjourned.]

[Additional material submitted for the record follows:]

MISSOURI PUBLIC SERVICE COMMISSION  
JEFFERSON CITY, MISSOURI  
July 1, 1999

The Honorable JOE BARTON, *Chairman*  
*Subcommittee on Energy and Power*  
*Committee on Commerce*  
*Room 2125, Rayburn House Office Building*  
*Washington, DC 20515-6115*

RE: H.R. 1117, Kansas Ad Valorem Tax Refunds

DEAR CHAIRMAN BARTON: This letter responds to various questions asked by members of the subcommittee during my remarks at the public hearing on Kansas Ad Valorem Tax Refunds on June 8, 1999. The specific areas of inquiry covered by this response are the following:

- 1) whether enactment of H.R. 1117 would violate the "takings clause" of the Constitution;
- 2) whether the refunds per customer are insignificant; and
- 3) whether the Missouri PSC has taken positions at the FERC opposing the grant of waivers of the ad valorem tax refund obligation in cases of hardship.

1. The Fifth Amendment, made applicable to the states through the Fourteenth Amendment, provides that "private property" shall not "be taken for public use, without just compensation." U.S. Const., Amend. V. In order to state a claim under the "Takings Clause," a plaintiff must first demonstrate that he possesses a "property interest" that is constitutionally protected. *See, Ruckelshaus v. Monsanto Co.*,

467 U.S. 986, 1000-01, 104 S. Ct. 2862 (1984). Thus, the fundamental question presented by the proposed legislation is whether the pipeline customers have a property interest in the accumulated interest associated with the court-ordered refund.

Controlling authority is found in a 1980 U.S. Supreme Court case, *Webb's Fabulous Pharmacies v. Beckwith*, 449 U.S. 155, 101 S. Ct. 446 (1980). In *Webb's*, the Florida Supreme Court had interpreted a statute in a manner that allowed clerks of county courts to keep the interest on monies deposited in interpleader cases. Noting that the principal sums deposited in interpleader funds were plainly private property, 449 U.S. at 162, 101 S. Ct. at 451, as were "[t]he earnings of the fund," 449 U.S. at 163, 101 S. Ct. at 452, the Court ruled that the Florida statute authorized takings in violation of the Fifth and Fourteenth Amendments, and was therefore unconstitutional.

In 1998, the U.S. Supreme Court again revisited the question of whether the interest generated by private funds is a property interest cognizable under the Takings Clause. See, *Phillips v. Washington Legal Foundation*, 118 S. Ct. 1925, 1928 (1998) (holding that interest earned on client funds in IOLTA accounts is the private property of the client.) Employing the "interest follows principal" rule,<sup>1</sup> the Court reaffirmed its earlier position in *Webb's*, noting that:

a State by ipse dixit, may not transform private property into public property without compensation simply by legislatively abrogating the traditional rule that 'earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property.' In other words, at least as to confiscatory regulations (as opposed to those regulating the use of property), a State may not sidestep the Takings Clause by disavowing traditional property interests long recognized under state law.

*Id.* at 1931 (citations omitted).

Finally, in *Blomberg v. Pinellas County*, 836 F. Supp. 839 (M.D.Fla. 1993), a case somewhat analogous to the current situation, a Florida District Court was asked to address whether a water utility customer who pays a deposit to the utility is entitled to the interest that accumulates on the deposit. Following *Webb's*, the court ruled that interest on the deposited funds was the customer's private property and that "an unconstitutional taking occurred when the Defendant failed to return interest to utility customers." *Id.* at 846.

In the case at hand, there is no dispute as to whether the ad valorem tax refund principal is the private property of pipeline customers. The dispute relates to the interest that has accrued on those funds since 1983. Under *Webb's* and its progeny, because the refund principal is the customer's private property, and interest follows the principal, the interest is also private property and therefore subject to traditional Takings clause protections. Thus, Congressional acts that redirect or otherwise nullify the interest payments to pipeline customers would likely run afoul of *Webb's*, and consequently, be found to be unconstitutional Takings.

2. Questions were raised and comments were made regarding the effect of ad valorem tax refunds on a typical natural gas customer. Contrary to others' statements that these refunds would "end up as a one-time deduction of a few cents off" a customer's gas bill, the impact of the ad valorem tax refunds on Missouri consumers is significant. Based on calculations by the staff of the Missouri PSC, if all owed ad valorem tax refunds were paid, each Missouri Gas Energy residential gas customer would receive a \$60-65 credit. This is approximately 9.5% of the average customer's annual gas bill.

3. Questions were raised concerning the position taken by the Missouri PSC in response to various petitions for adjustment of the obligation to make refunds of ad valorem taxes.

In the case of *M.A. Calvin*, Docket No. SA98-9-000, the Missouri PSC initially protested the petition for adjustment of the obligation to make ad valorem tax refunds on grounds that the petitioner failed to document financial hardship. In addition, the Missouri PSC contended that M.A. Calvin was not a first seller, but instead was a working interest owner. In this respect, it is the Missouri PSC's position that the first seller/operator, CLX Energy, Inc., is responsible for the ad valorem tax refunds attributable to all working interests in the well. On November 27, 1998, the Federal Energy Regulatory Commission ("FERC") granted the adjustment requested by M.A. Calvin. The Order denying Missouri PSC's petition for rehearing was issued on January 13, 1999. On March 12, 1999, the Missouri PSC filed its Petition for review in the United States Court of Appeals in Case No. 99-1103.

The Missouri PSC notes that Commissioner Hebert's concurring statement in the October 28, 1998 Letter Order (Attachment A) highlights the Missouri PSC's generic

<sup>1</sup> The Court noted that most states—Kansas and Missouri included—had similar common law understandings regarding the property rights associated with interest.

concern over the lack of information regarding the petitioner's financial status. Notwithstanding this concern, the Missouri PSC did not challenge the FERC's finding of hardship. The sole issue raised in the Missouri PSC's appeal is whether FERC erred by imposing a refund obligation on each individual interest owner rather than on the first seller/operator of the well. FERC's decision to impose a refund obligation on each interest owner departs from a longstanding practice, affirmed by the Court, of treating only the first seller/operator as the sole jurisdictional seller of gas from a well with multiple interest owners. *Sun Oil Company v. Federal Power Commission*, 256 F.2d 233 (D.C. Cir. 1958). Missouri PSC's position if adopted, would reduce the administrative burdens on small interest owners, pipelines, the Missouri PSC and the FERC.

In the case of *Sally L. Bone*, Docket No. SA98-21-000, the Missouri PSC protested the petition for adjustment from the obligation to make ad valorem tax refunds because the petitioner failed to provide documentation that she was financially unable to pay the refunds attributable to her ownership interest. In addition, the Missouri PSC protested the failure of petitioner to document the uncollectibility of refunds attributable to her other interest owner. On November 25, 1998, FERC granted the adjustment and the Missouri PSC did not appeal this decision.

In the case of *Continental Energy*, Docket No. SA98-101-000, the Missouri PSC protested the petition by Continental Energy for waiver of the ad valorem tax refund obligation because the petitioner had failed to document its claim of hardship and uncollectibility of refunds attributable to royalty interests. The Missouri PSC would not oppose the granting of this adjustment if adequate evidence of petitioner's financial hardship and inability to collect refunds from royalty owners is provided.

I hope this letter is responsive to the questions raised at the hearing. Should you need further information or assistance, please do not hesitate to contact me or my staff.

Respectfully submitted,

SHEILA LUMPE  
*Chair*

Attachment  
Copy to Members of the Subcommittee on Energy and Power

85 FERC ¶ 61,114  
 UNITED STATES OF AMERICA  
 FEDERAL ENERGY REGULATORY COMMISSION

Merleyn A. Calvin ) Docket No. SA98-9-000

(Issued October 28, 1998)

HÉBERT, Commissioner, *concurring*

When the Commission issued its Order denying generic petitions for adjustment of the Kansas ad valorem refunds and establishing procedures for payment, the Commission stated that it was aware that the obligation to make these payments "could present a serious financial problem to specific producers." <sup>1/</sup> Accordingly, the Commission indicated it would entertain requests for waiver of the obligation pursuant to NGPA section 502(c), if a producer could show how payment of the refund obligation would cause "special hardship, inequity, or unfair distribution of burdens." <sup>2/</sup> It appears clear to me that the obligation that a petitioner has under 502(c) then is to demonstrate to this Commission that payment of the Kansas ad valorem amounts would cause a "serious financial problem."

In a companion proceeding on this agenda the Commission made that very inquiry. In Mull Drilling Company, Inc. (Docket No. SA98-63-000) the Commission denied a request to amortize the petitioner's refund obligation since financial data submitted showed that the petitioner's cash-on-hand was sufficient to support payment of the refund obligation without causing a "special hardship, inequity, or an unfair distribution of burdens within the meaning of NGPA section 502(c)." However, I am concerned that during the review of the petitioner's request for waiver in the instant proceeding that the same knowledge about the petitioner's current financial status is not known. I believe that a proper analysis of any request for a special adjustment of a debt must include a consideration of the petitioner's current ability to pay the debt. I believe that an analysis which relies upon statements about past financial matters does not adequately respond to the NGPA section 502(c) standard.

<sup>2/</sup> Public Service Company of Colorado, 80 FERC ¶ 61,264, at 61,952-53 (1997).

<sup>3/</sup> Id.

Merleyn A. Calvin  
Docket No. SA98-9-000

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Accordingly, while I concur in the final decision to grant the petitioner a waiver of the Kansas ad valorem refund amounts, I believe that the Commission should process these requests in a more consistent manner and grant, or deny, such requests by holding all petitioners to the same standard of documentation.

Respectfully,

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Curt Hébert, Jr.  
Commissioner

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