STATE OF LOUISIANA
BOARD OF TAX APPEALS

COMPASS ENERGY OPERATING, LLC
PETITIONER

VERSUS **No. 9523D**

KIMBERLY ROBINSON, SECRETARY OF THE LOUISIANA DEPARTMENT OF REVENUE
RESPONDENT

JUDGMENT WITH WRITTEN REASONS

This matter came before the Board of Tax Appeals (the "Board") for hearing on February 10, 2021. Before this Board is the Petitioner, Compass Energy Operating, LLC ("Compass") contesting the assessment by Kimberly Robinson, Secretary of the Louisiana Department of Revenue (the "Department") of additional severance tax for the period of February 28, 2013 through June 30, 2014 (the "Audit Period"). The Department filed a *Motion for Summary* Judgment seeking a judgment from this Board upholding the assessment and dismissing Compass's claims. Compass filed a *Motion for Summary Judgment* seeking a judgment from this Board vacating and cancelling the Department's assessment. Presiding at the hearing was Judge Tony Graphia (Ret.), Chairman, with Board Members Cade R. Cole and Francis J. "Jay" Lobrano present. Participating in the hearing were Herbert "Chip" Hines, attorney for Compass, and Aaron Long, attorney for the Department. After the hearing, the case was taken under advisement. The Board now issues this judgment in accordance with the written reasons attached herewith.

IT IS ORDERED, ADJUDGED AND DECREED that the Department's *Motion for Summary Judgment* BE AND IS HEREBY GRANTED, and Compass' *Cross Motion for Summary Judgment* BE AND IS HEREBY DENIED.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that Judgment be rendered in favor of the Department and against Compass and that Compass' Petition BE AND IS HEREBY DISMISSED.

JUDGMENT RENDERED AND SIGNED at Baton Rouge, Louisiana, this 3rd day of June, 2021.

FOR THE BOARD:

JUDGE TONY GRAPHIA (RET.), CHAIRMAN
LOUISIANAN BOARD OF TAX APPEALS

STATE OF LOUISIANA
BOARD OF TAX APPEALS

COMPASS ENERGY OPERATING, LLC
PETITIONER

VERSUS **No. 9523D**

KIMBERLY ROBINSON, SECRETARY OF THE LOUISIANA DEPARTMENT OF REVENUE
RESPONDENT

WRITTEN REASONS FOR JUDGMENT

This matter came before the Board of Tax Appeals (the "Board") for hearing on February 10, 2021. Before this Board is the Petitioner, Compass Energy Operating, LLC ("Compass") contesting the assessment by Kimberly Robinson, Secretary of the Louisiana Department of Revenue (the "Department") of additional severance tax for the period of February 28, 2013 through June 30, 2014 (the "Audit Period"). The Department filed a *Motion for Summary* Judgment seeking a judgment from this Board upholding the assessment and dismissing Compass's claims. Compass filed a *Motion for Summary Judgment* seeking a judgment from this Board vacating and cancelling the Department's assessment. Presiding at the hearing was Judge Tony Graphia (Ret.), Chairman, with Board Members Cade R. Cole and Francis J. "Jay" Lobrano present. Participating in the hearing were Herbert "Chip" Hines, attorney for Compass, and Aaron Long, attorney for the Department. After the hearing, the case was taken under advisement. The Board now issues judgment for the following written reasons.

I. Facts and Background

Compass is an independent producer and seller of oil and natural gas (sometimes natural gas is simply referred to as "gas"). Compass owns and operates a number of oil and gas wells with related production facilities in the Vernon field located primarily in Jackson Parish. Sometime in the latter half of 2014/beginning of 2015, the Department conducted a severance tax audit of Compass for the Audit Period and ultimately determined that Compass had failed to include certain "lost and unaccounted for" gas in its severance tax base. On September 25, 2015, the Department assessed Compass with additional severance taxes (and statutory interest) of $140,117.94. Compass timely filed this Petition with the Board.

At issue is the gas used by Compass's wholly owned entity Vernon Gathering, LLC ("Vernon") to fuel Vernon's compressors and other related equipment. Such gas is sometimes referred to as the "Fuel Gas". Compass did not include the Fuel Gas used by Vernon in its gathering services in Compass's severance tax base based on its assertion that severance tax was not due on the Fuel Gas pursuant to La. R.S. 47:633(9)(e)(iv).[1] Specifically, during the Audit Period, Vernon performed gas gathering services for Compass whereby Vernon provided its services, equipment, and pipelines to gather Compass's gas from numerous "points of receipt" (typically at or near Compass's producing wells) to numerous "points of delivery" (typically to larger pipelines and

[1] La. R.S. 47:633(9)(e)(iv) provides: [Severance] tax shall not accrue on the severance of gas ... **used by the operator** ... **on leases operated by such operator for fuel** in connection with the operation and development for or production of oil and gas in the field where produced. Gas used for fuel by an operator shall include gas used for heating, separating, producing, dehydrating, compressing, and pumping of oil and gas in the field where the gas is produced provided such gas in not otherwise sold

transmission stations owned by larger pipeline companies such as Gulf South Pipeline Co, L.P. and Tennessee Gas Pipeline).

Vernon provided the gathering services pursuant to a written agreement between Vernon and Exco Partners Operating Partnership, LP (the predecessor in interest to Compass) dated March 30, 2007 (the "Gas Gathering Agreement"). Under Article II of the Gas Gathering Agreement, Compass (defined in the Agreement as the "Shipper") agreed that it would use Vernon as its exclusive gas gatherer in the Vernon Field and that all gas produced from the field would be delivered and sold through Vernon's gathering system, except: (a) gas used by Compass in the production of its wells (i.e., injection gas); (b) any gas delivered to royalty owners in satisfaction of lease and override obligations; and (c) gas used by Compass to produce its wells, including field gathering, field compression and/or gas lifting, prior to delivery to the point of receipt. Vernon had the right to reject certain gas under the "curtailment procedures" in Article 3.3 of the Gas Gathering Agreement and further had the right in Article 3.4 to commingle gas Vernon received from sources other than Compass.

The Gas Gathering Agreement further provided in Article 5.2 that Compass would have custody of the gas prior to the delivery to the point of receipt, at which point Vernon would take custody of the gas and thereafter be responsible for any damages or injuries caused by or related to the gas until delivered to the point of delivery. Under Article 6.1, Vernon was not obligated to accept certain gas in its system that failed to meet certain specifications (such as containing excess sulphur and

liquids). The fees set out in Article VII of the Gas Gathering Agreement provide for an initial fee due by Compass to Vernon of 27 cents per MMBtu, subject to adjustment in accordance with Article 7.3. Further, Article 7.4 grants Vernon the right to use gas delivered by Compass into Vernon's gathering system for Fuel Gas as required to support Vernon's gas gathering services without any additional compensation to Compass.

Article VIII of the Gas Gathering Agreement requires Vernon to accurately measure the volume of gas delivered by Compass into Vernon's system though meters installed, maintained and operated by Vernon. Specifically, Article 8.4 requires Vernon to measure specific gravity at least once a year. Article 8.7 requires Vernon to determine heating value (to calculate MMBtu). Article 9 sets forth the terms and conditions by which Compass pays Vernon for its gas gathering services, including invoicing, terms for payment, and the imposition of an interest rate for late payment. Article 9.4 specifically grants to Vernon the right to seek security for open invoices in the event reasonable grounds for insecurity rise, including a letter of credit, bond, prepayment, or a security interest in an asset acceptable to Vernon. Article 12.1 requires that Vernon and Compass assume full responsibility for the maintenance and operation of their respective properties, and further requires cross indemnification by each to the other for any liability, claim, or injury brought against one resulting from a loss caused the other's property[2].

---

[2] Also attached to the affidavit of Donny Hall, chief financial officer for Compass Production Partners, LP, was a Services Agreement dated May 1, 2007 by and between Exco Resources, Inc. and Vernon whereby Exco Resources, Inc. was to provide employees and management services to Vernon as an independent contractor in the operation of the Vernon gas gathering system. The record is unclear whether this agreement was in effect during the Audit Period, and neither the Department nor Compass referred to this Agreement specifically either in their respective Statements of Uncontested Facts or in their briefing of this matter. We assume the agreement was therefore not in effect.

Additional undisputed material facts occurring within or relevant to the audit period are as follows: Vernon owned the pipelines and transmission equipment used in its gathering system. Vernon was a disregarded entity of Compass for federal and state income tax purposes, meaning that Compass reported all of Vernon's income and expenses on its own federal and state income tax returns. Vernon did not have any employees.[3] The fee charged by Vernon to Compass for the gas gathering services was equal to Vernon's costs - i.e., there was no mark up or profit made by Vernon on the provision of the gas gathering services to Compass. Vernon provided gas gathering services to unrelated third party operators at a profit.

II. Law and Analysis

The only issue presented in this case is whether the Fuel Gas delivered and transferred by Compass to Vernon is subject to severance tax by the severer of that gas – Compass Energy? While the Department and Compass both filed their own statements of uncontested material facts in this case, neither party has alleged that any facts are in dispute. Therefore, we find that the resolution of this case turns on the pure legal issue of whether La. R.S. 47:633(9)(e)(iv) exempts the Fuel Gas used by Vernon to power and operate its gas gathering system from severance tax.

[3] The implication from the affidavit of Donny Hall and Compass's Statement of Uncontested Facts is that it was Compass's employees that provided the labor necessary for Vernon to perform under the Gas Gathering Agreement. However, with the possible exception of the May 1, 2007 agreement, nothing submitted by Compass establishes that any employee or independent contractor of Compass provided labor or other services to Vernon.

Louisiana Constitution Article VII, Section 4(B), codified at La. R.S. 47:631, authorizes the imposition of a tax on natural resources. The Constitution states:

> Taxes may be levied on natural resources severed from the soil or water, to be paid proportionately by the owners thereof at the time of severance. Natural resources may be classified for the purpose of taxation. Such taxes may be predicated upon either the quantity or value of the products at the time and place of severance. No further or additional tax or license shall be levied or imposed upon oil, gas, or sulphur leases or rights.

La. R.S. 47:631 and La. R.S. 47:632, in pertinent part, provide:

> Section 47:631. Imposition of tax
>
> Taxes as authorized by Article VII, Section 4 of the Constitution of Louisiana are hereby levied upon all natural resources severed from the soil or water, including all forms of timber, including pulp woods, turpentine, and other forest products; minerals such as oil, gas, natural gasoline, distillate, condensate, casinghead gasoline, sulphur, salt, coal, lignite, and ores; marble, stone, sand, shells, and other natural deposits; and the salt content in brine.
>
> Section 47:632. Taxes payable by owners; lien and privilege created
>
> A. These taxes shall be paid by the owner or proportionately by the owners thereof at the time of the severance and become due and exigible monthly. . .

Further, La. R.S. 47:633 provides several exemptions from the imposition of the severance tax. The exemption pertinent to resolution of this matter is La. R.S. 47:633(9)(e)(iv) (the "Fuel Gas Exemption"), which provides in part the following:

> [Severance] tax shall not accrue on the severance of gas ... **used by the operator ... on leases operated by such operator for fuel** in connection with the operation and development for or production of oil and gas in the field where produced. Gas used for fuel by an operator shall include gas used for heating, separating, producing, dehydrating, compressing, and pumping of oil and gas in the field where the gas is produced provided such gas in not otherwise sold." (Emphasis added).

Compass advances two arguments as to why the Fuel Gas used by Vernon in its gas gathering system is not subject to the severance tax. First, Compass argues that the constitutional prohibition found in Louisiana Constitution Article VII, Section 4(B) gainst the levy of an additional or fee tax on the severance of oil and gas prohibits the imposition of the severance tax in this case on the Fuel Gas. Second, Compass argues that under a "substance over form/alter ego" analysis, Vernon's separate existence as an entity should be disregarded in this matter. If correct, Compass would thus be the "user" of the Fuel Gas, qualifying it for the Fuel Gas Exemption.

The Department argues that Vernon is an entity separate and distinct from Compass and therefore the Fuel Gas used by Vernon in the provision of its gas gathering services is not gas "used by the operator . . . on leases operated by such operator." Thus, the Fuel Gas Exemption would not available to Compass and the severance tax on the Fuel Gas transferred to Vernon would be payable due by Compass. For the following reasons, the Board agrees with the Department that the assessment is correct.

A motion for summary judgment will be granted after an opportunity for adequate discovery "if the motion, memorandum, and supporting documents show that there is no genuine issue of material fact and that the mover is entitled to judgment as a matter of law." La. Code Civ. Proc. art. 966(A)(3). A material fact is one whose existence or absence determines the outcome of a cause of action. *Davis v. Hixson Autoplex of Monroe, LLC*, 51, 991, p. 5 (La. App. 2. Cir. 5/23/18), 249 So.3d

177, 181. Any doubt as to a dispute regarding a genuine issue of material fact must be resolved against granting the motion and in favor of a trial on the merits. *Orleans Parish Sch. Bd. v. Lexington Ins. Co.*, 2011-1720, p. 9 (La. App 4. Cir. 8/22/12), 99 So.3d 723, 729.

However, once the motion for summary judgment has been properly supported by the moving party, the non-moving party must produce evidence of a material factual dispute or the motion will be granted. *Arceneaux v. Lafayette Gen. Med. Ctr.*, 2017-516, p. 4-5 (La. App. 3 Cir. 7/26/17), 248 So.3d 342, 346. The burden of proof rests with the mover, but if the mover will not bear the burden of proof at trial on the issue that is before the court on the motion for summary judgment, the mover's burden does not require him to negate all essential elements of the adverse party's claim, action, or defense, but rather to point out the absence of factual support for one or more essential elements to the adverse party's claim. La. Code. Civ. Proc. art. 966(D)(1).

Both Compass and the Department conducted substantial written discovery in this matter, with the result being that both the Department and Compass filed Motions for Summary Judgment. Neither party disputes any material fact in this case; thus, resolution of this case on summary judgment is appropriate.

A. ARE COMPASS AND VERON DISREGARDED ENTITIES FOR PURPOSES OF THE SERVEANCE TAX?

First, Compass argues that the Board should disregard the separate identity of Vernon, Compass's wholly owned subsidiary company, and in turn producing the result that Compass was the user of

the Fuel Gas in its capacity as the operator of the wells and leases, and thus such Fuel Gas is exempt from severance tax. The Board does not agree with Compass's characterization of Vernon as a disregarded or meaningless entity for this purpose.

In the context of the severance tax, this issue is *res nova*. However, there are several reported cases where the courts have considered whether sales tax should be imposed on transfers of tangible property (or taxable services rendered) between affiliated entities, and we find no meaningful legal distinction between the severance tax and the sales tax in this analysis. Therefore the Board relies on those decisions in these written reasons and our judgment in this case.

A substantial body of jurisprudence addresses the "substance over form" doctrine in pursuit of debtor liability and whether the veil will be pierced and the separate identity of an entity disregarded. See, e.g., *Riggins v. Dixie Shoring Co.,* No. 1991-0963 (La. 1992), 590 So. 2d 1164 and *Ogea v. Merrit* No. 2013-1085 (La. 2013), 130 So. 3d 888), and their progeny. However, the jurisprudence addressing this same issue in the context of state and local taxation is limited and less developed than in the typical "piercing the veil/substance over form" case. Further, unlike typical "substance over form" cases where an entity and its owners are asking that a court respect and recognize the separate existence of a legal entity to defend against a creditor's attempt to pierce the corporate veil, in a state and local tax case it is typically the taxpayer seeking to disavow the separate and distinct nature of its own entity in an effort to disregard the transaction for taxation purposes. In other words, it is the taxpayer

asking the courts to collapse and ignore an otherwise taxable transaction between two separate, albeit related, entities. Given the fact sensitive nature of the analysis, a brief review of the jurisprudence is helpful.

In *Associated Hospital Services, Inc. v. Louisiana Department of Revenue and Taxation,* No. 1991-0475 (La. 1991), 588 So. 2d 356, the only Louisiana Supreme Court case to analyze this issue in the context of the sales tax, the issue before the court was whether a non-profit hospital service corporation, wholly owned by its hospital members, was required to collect and remit sales taxes on the provision of laundry services to its owners. The taxpayer argued that under their unique circumstances, the corporate veil should be pierced and the identity of the taxpayer disregarded from its shareholders, thus rendering the transactions non-taxable. In so arguing, the taxpayer cited two Louisiana cases: *Cajun Contractors, Inc. v. Department of Revenue and Taxation,* (La. App. 1st. Cir. 1987), 515 So. 2d 625 and *United Companies Printing Co. v. City of Baton Rouge,* (La. App. 1st Cir. 1990), 569 So. 2d 186.

In rejecting the taxpayer's argument, the court factually distinguished the facts of *Cajun* and *United Cos. Printing* from the facts in *Associated Hospital Services.* In *Cajun,* the court observed that the partnership and its related entity, Cajun Equipment, were treated as a single entity for insurance, bonding and federal taxation purposes. Further, all of the subsidiary's clerical work was performed by the employees of the parent, and the two entities never entered into a formal written agreement regarding the alleged taxable transaction. The court also distinguished *United Cos. Printing* where the parent kept all the

accounting records, supplied the employees that carried out the subordinate functions, made purchases for the subsidiary, and allowed the subsidiary to occupy the parent's office building rent free. In addition, the subsidiary in *United Cos. Printing* had no bank account of its own and it owned no assets.

After distinguishing these cases relied upon by the taxpayer, the court then applied the factors it deemed determinative of the issue. First, it noted that the taxpayer was formed pursuant to Articles of Incorporation as required by law. There was a written agreement between the taxpayer and its owners for the provision of laundry services by the taxpayer. The taxpayer owned the assets (land and laundry plant) used in its business, had its own employees, made purchases, borrowed money and paid its own bills. The court also observed that although there was no markup and thus no profit made by the taxpayer on the transaction, the sales tax statute was not drafted to tax only profitable sales, and thus the lack of a profit was not relevant to the issue.

The Court also relied heavily on the universally accepted legal concept that a corporation is an entity separate and distinct from its owners, and applied that accepted premise to the Louisiana sales tax law, holding:

> The laundry service corporation was a legal entity or person separate from the hospital corporations by which it was organized and owned. The sales tax statute requires the collection of a sales tax when one person provides laundry service to another for consideration. It defines the concept of a legal person or entity no more narrowly than does the general law of persons. Accordingly, it does not appear to have been the legislative aim to dispense with the imposition of sales taxes upon transactions between closely related persons,

whether natural or legal. *Associated Hospital Services, Inc.* supra at 356.

Finally, as additional support for its decision, the court cited the general federal income tax rule that "when a taxpayer has chosen to do business as a corporation, it must accept the tax disadvantages of that form and will not be heard to deny the separate existence of that corporation." *Higgins v. Smith,* 308 U.S. 473, 60 S. Ct. 355, 84 L. Ed. 406 (1940).

Similarly, in *Hilton Hotels Corp. v. Traigle,* No. 1978-11997 (La. App. 1st Cir. 1978), 360 So. 2d 245, the First Circuit considered whether transactions involving the transfer of hotel supplies and equipment between Hilton and its wholly owned subsidiary Hotel Equipment Corporation were subject to local sales tax. The taxpayer in *Hilton* argued that its wholly owned subsidiary should be disregarded for sales tax purposes, with the result being that no sales tax would be due on the sale of equipment and other items between them. The court rejected the argument and found the transaction taxable. In a brief analysis, the court found that both corporations were separate and distinct legal entities, the transactions in question were fully documented, the subsidiary corporation had its own employees, and the subsidiary corporation had its own corporate officers (albeit the same officers as the parent). Similar to the court's findings in *Associated Hospital Services, Inc.,* supra, the court recognized that "[i]t ill behooves Hilton to attempt to disregard the corporateness of its subsidiary when it is in its interest to do so, while still obtaining whatever benefits flow from conducting business as separate corporations." *Hilton Hotels Corp.,* supra, at 246.

Unlike *Associated Hospitals* and *Hilton*, the facts of *United Cos. Printing*, supra, convinced the court to disregard the separate existence of the two entities. The City of Baton Rouge assessed sales taxes on the sale of printed forms from the taxpayer to its parent corporation, United Companies Financial Corporation. Again, the issue was whether the taxpayer would be treated as an entity separate from its parent corporation. The factors relied on by the court in its finding that the entities should be disregarded are as follows: (1) all of the accounting records were kept by the parent; (2) the parent company owned the building that housed the taxpayer and no rent was paid; (3) the parent company purchased all of the forms and other raw materials for the taxpayer to make the forms; (4) there was no mark up on the price on the sales from the taxpayer to the parent; (5) the parent company paid the taxpayer via check, which was endorsed back to the parent, as the taxpayer had no separate checking account; (6) the parent company paid for the printing equipment; and (7) the parent and the taxpayer filed a consolidated tax return. In its decision, the court distinguished *Hilton Hotels Corp.*, supra, and *Cajun Contractors,* supra, and concluded that the sale of the goods constituted intercompany transfers and thus were not sales and not taxable events.[4]

---

[4] In support of its position, Compass also cites *Cajun Contractors,* supra, and *St. Gabriel Industrial Enterprises, Inc. v. Broussard,* 1991-0876 (La.App. 1st Cir. 1992), 602 So. 2d 1087. In *Cajun,* supra, the factors in favor of disregarding the existence of a partnership owned by three shareholders of Cajun, the taxpayer corporation, were: (1) for insurance, bonding and federal taxation purposes, the partnership and Cajun were treated as a single entity; (2) the partnership had no separate employees; (3) All of the partnership's clerical work was performed by Cajun's employees; (4) the payments made by Cajun to the partnership were for the exact amount due on the notes used to purchase the equipment; and (5) there was never a written lease between Cajun and the partnership. Similarly, in *St. Gabriel Industrial Enterprises, Inc. v. Broussard,* No. 1991 0876 (La.App.1st.Cir. 1991), the factors convincing the court to disregard the separate existence of two corporations owned by the same shareholder were: (1) the lack of employees or other attributes of autonomy except the formality of a corporate charter; (2) the lack of customers other than its related entity; and (3) the lack of a written lease between the entities.

With the above cases in mind, we turn to the instant case and whether Vernon should be disregarded from its parent Compass. We find that the following factors preponderate in favor of recognizing and treating Vernon as an entity separate and distinct from its parent Compass, thus rendering Compass liable for the severance tax on the Fuel Gas:

1. Vernon provides the gathering services pursuant to a written agreement;

2. Vernon has the right to reject certain gas under the "curtailment procedures" in Article 3.3 of the Gas Gathering Agreement;

3. The Gas Gathering Agreement provides that Vernon would take custody of the gas and be responsible for any damages or injuries caused by or related to the gas until delivered to the point of delivery;

4. Vernon is not obligated to accept certain gas in its system that fails to meet certain specifications (such as containing excess sulphur and liquids);

5. Vernon charges Compass for the services provided by Vernon pursuant to the Gas Gathering Agreement which includes the terms and conditions by which Compass pays Vernon for its gas gathering services, including invoicing, terms for payment, and the imposition of an interest rate for late payment;

6. Article 9 of the Gas Gathering Agreement sets forth the terms and conditions by which Compass pays Vernon for its gas gathering services,

including invoicing, terms for payment, and the imposition of an interest rate for late payment;

7. Article 9.4 of the Gas Gathering Agreement specifically grants to Vernon the right to seek security for open invoices in the event reasonable grounds for insecurity rise, including a letter of credit, a bond, a prepayment, or a security interest in an asset acceptable to Vernon;

8. Article 12.1 of the Gas Gathering Agreement requires that Vernon and Compass assume full responsibility for the maintenance and operation of their respective properties;

9. Vernon, not Compass, owned the pipelines and transmission equipment used in its gathering system; and

10. Vernon provides gas gathering services to unrelated third party operators at a profit.

The relationship between Compass and Vernon is more akin to the relationship between the parties in *Associated Hospital Services* and *Hilton Hotels* than the parties in *Cajun Contractors, St. Gabriel Industries,* and *United Cos. Printing.* Other than the actual formality of a recorded partnership agreement and a corporate charter, neither of the parties in *Cajun* and *St. Gabriel Industries* had any attributes of an active and autonomous legal entity. In this case, Vernon maintained a separate autonomy, complete with a written agreement containing many arm's length terms and conditions. Vernon also owned its own equipment and assumed real risks in the provision of its services. In addition, unlike

the parties in *Cajun* and *St. Gabriel,* Vernon also provided the same gas gathering services to unrelated third parties.

Compass points to certain factors in favor of Vernon's disregarded existence from Compass. Compass asserts that the fact that Vernon provided the gas gathering services to Compass at no profit is a factor in its favor, citing *United Cos. Printing,* supra. However, in *Associated Hospitals,* supra, the La. Supreme Court commented that while "[i]t is true that no profit was made on the transaction to be taxed, but the sales tax statute is not drawn to tax only profitable sales [citation omitted], so the fact that no profit was made cannot be determinative of whether a sales tax is due." We note *Associated Hospitals,* supra, is the only La. Supreme Court case addressing this particular issue in the context of a tax matter, and that the case was decided after both *Cajun Contractors* and *United Cos. Printing.*

In addition to the lack of a profit, Compass relies on the fact that Vernon was a disregarded entity for federal and state income tax purposes. Compass cites *United Cos. Printing* and *St. Gabriel Industries* for that proposition. We note that this is but one of the factors in determining this issue, and further note that in 1992, the legislature enacted La. R.S. 12:1368, which is the basis for disregarding certain limited liability companies for state income tax purposes, but not for any other purposes, including sales tax and severance tax purposes. As the court in *Associated Hospitals, Inc.* ruled, no exception is found in the statutes that collapse two or more entities for purposes of the fuel gas exceptions to the severance tax. We find that had the legislature intended

to exempt the transaction from the severance tax, it would have expressly done so.

Finally, although some of the factors in this case favor Compass's position, the determination of whether Vernon's separate existence can be disregarded for severance tax purposes is based on a totality of the facts and circumstances, and the burden is on the taxpayer to establish that Vernon's separate existence should be ignored. We find that even though some of the factors do in fact favor Compass, the overall relationship between Compass and Vernon is best described as an arm's length relationship between two separate and distinct legal entities. As stated by the court in *Associated Hospital Services,* supra, the sales tax statute "defines the concept of a legal person or entity no more narrowly than does the general law of persons." We agree, and therefore find in favor of the Department on this issue.

B. DOES THE DEPARTMENT'S ASSESSMENT OF ADDITIONAL SERVERANCE TAX VIOLATE LA. CONST ART. VII, SEC. 4(B)?

Compass argues that Constitution Article VII, Sec. 4(B), La. R.S. 47:633(9)(e)(iv), and prior jurisprudence mandate that the Fuel Gas was "used by" Compass since it retained ownership.[5] Taxpayer cites *Hanover Compressor Co. v. Department of Revenue and Taxation*, 2002-0925 (La. App. 3 Cir. 2/5/03) 838 So.2d 876, and *Bridges v. Production Operators, Inc.*, 2007-0648 (La. App. 4 Cir. 12/12/07) 947 So.2d 54, among other cases. Taxpayer argues these sales tax cases support that "use" for severance tax purposes "cannot be so broad as to constitute any transfer

[5] Compass only asserts it retained ownership for severance tax purposes. The ownership for sales/use tax purposes is not an issue before this Board.

of possession because in holding so [the Board] would expose taxpayers to multiple taxation." Taxpayer summarizes its position by stating:

> [B]ecause the gas would be subject to use tax for Louisiana sales and use tax purposes it is therefore not subject to severance tax under the Louisiana Constitution.

The correct application of the law is the following: Louisiana Severance tax would not be due in an instance where Louisiana sales or use tax is due on gas used by compressors / gatherers.

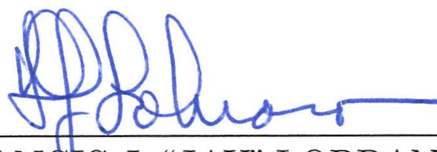
Compass's argument is misplaced. The Louisiana Constitution provides the State with the right impose *severance tax* on natural resources, including gas, unless a specific exemption applies. La. Const. art. VII, Sec 4(B); *See also* La. R.S. 67:631. It is true that the imposition of any "further or additional tax or license" on natural resources for which severance tax has already been paid may be disallowed until that resource is purchased by a third party. *See United Gas Pipe Line Co. v. Whitman*, 390 So.2d 913 (La. App. 2 Cir. 10/28/1980) 390 So.2d 913. La. Const. Art. VII, Sec. 4(B) prohibits the imposition of any other tax against the producer other than severance tax on oil or gas. If the exemption does not apply, any notion that the imposition of *severance tax* against the Taxpayer is unconstitutional is false since the tax issue in this case is the severance tax and not a sales tax or any other prohibited tax on the severance of the gas.

Further, the plain reading of the phrase "used by the operator" requires the consumption of the gas by the operator itself, and not

another party.[6] Compass was the operator of the wells, and concedes that Vernon, the party consuming the gas, was not the operator of the wells. Compass did not use the gas within the plain meaning of Louisiana Revised Statute 47:633(9)(e)(iv). Further, La. Const. Art. VII, Sec. 4(B) prohibits the assessment of a tax other than the severance tax against the producer, and in this case it is undisputed that the tax at issue is the severance tax and therefore not prohibited. Compass's argument is without merit.

Thus signed in Baton Rouge, Louisiana, this 3rd day of June, 2021.

FOR THE BOARD:



FRANCIS J. "JAY" LOBRANO, BOARD MEMBER
LOUISIANAN BOARD OF TAX APPEALS

[6] La. R.S. 47:633(9)(e)(iv) states tax shall not accrue on the severance of gas ... "used by the operator as described in R.S. 47:640 on leases operated by such operator..." La. R.S. 47:640 addresses reports by the purchasers and does not define the phrase "used by the operator."