09-0273

In the
Supreme Court of Texas

MIDLAND CENTRAL APPRAISAL DISTRICT,
Petitioner,

v.

BP AMERICA PRODUCTION COMPANY; AMERADA HESS TRADING COMPANY;
CHEVRON USA, INC.; CHEVRON TEXACO PRODUCTS COMPANY;
CHEVRONTEXACO GLOBAL SUPPLY AND TRADING COMPANY,
TEPPCO CRUDE OIL, LLC; AND TEPPCO CRUDE P/L LLC,
Respondent.

On Petition for Review from the
Eleventh Court of Appeals at Eastland, Texas

AMICUS CURIAE BRIEF OF THE
TASB LEGAL ASSISTANCE FUND

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A substantially identical brief has been submitted in *Harrison Central Appraisal District v. Peoples Gas, Light, and Coke Co.*, No. 09-0053

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STATEMENT OF INTEREST OF AMICUS CURIAE

Nearly 800 public school districts in Texas are members of the Texas Association of School Boards Legal Assistance Fund ("TASB Legal Assistance Fund"), which advocates the interest of school districts in litigation with potential statewide impact. No other entity has paid for any part of the preparation of this brief.

TASB Legal Assistance Fund is governed by three organizations:

- Texas Association of School Boards, Inc., a non-profit corporation whose members are the approximately 1,030 public school boards in Texas;[1]
- Texas Association of School Administrators, which represents the State's school superintendents and other administrators responsible for carrying out the education policies adopted by their local boards of trustees; and
- Texas Council of School Attorneys, which comprises attorneys who represent more than ninety percent of the public school districts in Texas.

[1] As locally elected boards of trustees, TASB's members are responsible for the governance of Texas public schools. *See* TEX. EDUC. CODE §11.151(b) & (d).

No. 09-0273

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BP AMERICA PRODUCTION COMPANY; AMERADA HESS TRADING COMPANY; CHEVRON USA, INC.; CHEVRON TEXACO PRODUCTS COMPANY; CHEVRONTEXACO GLOBAL SUPPLY AND TRADING COMPANY, TEPPCO CRUDE OIL, LLC; AND TEPPCO CRUDE P/L LLC,
Respondent.

On Petition for Review from the
Eleventh Court of Appeals at Eastland, Texas

AMICUS CURIAE BRIEF OF THE TEXAS ASSOCIATION OF SCHOOL BOARDS LEGAL ASSISTANCE FUND

TO THE HONORABLE SUPREME COURT OF TEXAS:

This rehearing is important to the Texas local government entities that depend on property taxes for support. The jurisprudence is now confused — with two Texas courts of appeals reaching results at odds with the prevailing view of federal law, and with basic principles of Texas tax law. Struggling under this confusion will hurt local school districts and the state education-funding system. The Court should grant rehearing in this case and in *Harrison Central Appraisal District v. Peoples Gas, Light, and Coke Co.*, No. 09-0053, to resolve this confusion and state clearly which competing view of federal law applies in Texas courts.

SUMMARY OF THE ARGUMENT

These cases will be felt statewide. In the Texarkana and Eastland districts, local governments won't be able to levy a fair tax on this class of commercial property, shifting that burden to remaining taxpayers and, ultimately, to other school districts through the statewide school-funding system. In other appellate districts, local governments will face a dilemma: meeting the constitutional command for tax equity will subject them to repeated and costly litigation until this Court takes up the issue.

Texas jurisprudence also suffers. First, these cases announce a dangerous principle that a state cannot impose property taxes without also showing a nexus to some other business activity (like might be required for a franchise tax). That basic mistake about the Dormant Commerce Clause invites mischief and threatens significant damage to property tax rolls. Second, these cases have clumsily displaced the first *Complete Auto* prong with the older "continuity of transit" analysis. If this reading is to be believed, *Complete Auto* is a test the state can never win ("if it's in commerce, then it lacks nexus and fails the first prong of the test"), rolling back decades of federal law.

These petitions frame the problem well, and their contrasting facts offer a better vehicle to reach a clear rule than any single, later petition is likely to present. Waiting would just invite more confusion. Until the Court resolves the core issues, the lingering uncertainty will make planning difficult for taxing authorities and property owners. Indeed, several pipelines have filed an amicus brief in this Court complaining that they do not know the tax status of pipelines under the prevailing federal rule adopted by a sister court and advocated by the U.S. Solicitor General. Granting rehearing is a perfect chance to provide clarity for both government and industry.

ARGUMENT

I. THESE CASES WILL HURT THE EDUCATION-FUNDING SYSTEM.

As the Court knows all too well, Texas public education depends on the local property taxes at issue in these petitions. Although just two appraisal districts appear before the Court today, these holdings will ripple through the system of recapturing revenues from property-rich districts and shifting it to property-poor districts. Petroleum assets are particularly valuable property. The facilities involved in these cases collectively hold hundreds of millions of dollars worth of inventories.[2]

If the misguided decisions below are ultimately blessed with a petition denial, tax lawyers would be remiss not to bring similar challenges around the state. The uncertainty could lead to uneven application of property tax. TEX. CONST. art. VIII, §1(a)-(b). And as the overall tax rolls contract, more stress will fall on other sources for funding the constitutionally required system of public education. TEX. CONST. art. VII, §1. The needlessly narrow view of federal law adopted by the Texarkana and Eastland Courts makes the Legislature's job even tougher.

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[2] *See* Petition for Review, *Midland Cent. Appraisal Dist. v. BP America Prod. Co.*, No. 09-0273, at 2 (May 20, 2009) (roughly 3 million barrels of oil continuously present at the Midland facility); *Peoples* op. at 3 ("[T]he District assessed Peoples' portion of the gas at North Lansing, for those years, at values exceeding nine million [for 2002], forty million [for 2003], and forty-three million dollars [for 2004], respectively.").

Prudence favors granting rehearing instead of waiting for some future case to percolate through the property-tax system. That delay has a real cost. Local authorities within these two appellate districts would just be out of luck. And those elsewhere in the state would face costly litigation before contested taxes could reach the schools.

The doctrine of the Dormant Commerce Clause is a default for allocating power between the federal level and state legislatures. Through their antiquated understanding of this doctrine, the Texarkana and Eastland courts have taken a far more restrictive view of Texas authority than has the federal government. There is no reason to tie the hands of local authorities or to make the Texas Legislature seek Washington's permission to impose the same property taxes that sister states already do.

II. UNLESS THE COURT GRANTS REHEARING, THESE DECISIONS WILL CONFUSE TEXAS JURISPRUDENCE.

The courts below went to great lengths to circumvent the usual test of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Instead, the property owners advanced — and the courts of appeals accepted — sweepingly broad rationalizations to either ignore it or render most of its elements surplus.

That strategy raised the stakes. It's not just whether the courts below were wrong (they were); it's how they were wrong. In addition to placing Texas at odds with its neighbor on an important question of federal law, the decisions below have confused Texas jurisprudence about two broad questions critical to the property-tax system:

- Do local property taxes require jurisdiction both over the property being taxed and the taxpayer personally? (The courts below answered "yes," threatening the constitutional foundation of property taxes.)

- Can any tax imposed on property traveling in interstate commerce ever pass constitutional muster under *Complete Auto*? (The Eastland Court answered "no" by making the old "in transit" test completely displace the first element of *Complete Auto* so that the state can never win.)

These holdings were central to the decisions below and, unless the Court grants rehearing, will define the path of future property-tax litigation in Texas.

A. Testing nexus against a taxpayer's business <u>activities</u> in order to tax its <u>property</u> is a terrible precedent for the Texas property-tax system.

1. This was the key to the holdings below.

Both decisions below framed "substantial nexus" in terms of the state's nexus with the taxpayer rather than its nexus with the property taxed.

The *Peoples* analysis focused on the property owner's lack of "offices in Texas" or "employees" here, as well as the decision-making process that led to the gas being stored in Texas. *Peoples* op. at 16-17. Its ultimate conclusion was that "[s]uch a connection is too tenuous to subject Peoples to ad valorem taxation in Texas." *Id.* at 16.

In the middle of that analysis is a critical concession that deserves a much closer look: "If we were to look strictly at the generic act of storing gas in a reservoir in Harrison County, it might appear that such activity would have a substantial nexus with the State." *Id.* at 16. This sentence should dispel any doubt about the nature of the error: Had the *Peoples* opinion (correctly) been looking for a nexus to the property itself — instead of erroneously looking to the identity of the taxpayer — then the first prong of *Complete Auto* would have been easily met.

A few months later, the *BP America* court fell into precisely the same error, citing and relying upon this aspect of *Peoples*. *BP America* op. at 9. It (accurately) described the holding of *Peoples* as turning on whether "the gas owner's activities in Texas and its connection to Texas were too tenuous to create a substantial nexus." *Id.* (emphasis added) (citing *Peoples* op. at 17).

Continuing along the same thread, the *BP America* court made clear how central this distinction was to its holding "Although the oil itself had a substantial nexus with this state . . . the 'activity' being taxed had no such nexus. The activity essentially being taxed in this case was the ownership of oil . . . ." *BP America* op. at 10 (emphasis added). In other words, the court recognized that the property itself did have a substantial nexus with the state. Its contrary holding rested on the argumentative move of substituting the taxpayer for the property being taxed.

2. This error will confuse the jurisprudence.

The Dormant Commerce Clause looks for a substantial nexus "between a state and the person, property, or transaction it seeks to tax." *Allied-Signal, Inc. v. Director, Division of Taxation*, 504 U.S. 768, 777 (1992) (quoting *Miller Bros. v. Maryland*, 347 U.S. 340, 344-45 (1954)). Parsing that sentence, the nexus can be with the "property . . . it seeks to tax." *Id.* And the Supreme Court has connected these dots explicitly: "Of course, the situs of property may tax it regardless of the citizenship, domicile, or residence of the owner." *Miller Bros.*, 347 U.S. at 345 (emphasis added).

The difference between power to tax property and power to tax a person is fundamental. The courts below should have asked how the property itself related to Texas, rather than giving dispositive weight to whatever name happened to be slapped on the property by the shipper. That would have tracked the analysis employed by the U.S.

Solicitor General, which looked to "the nexus between Oklahoma and the 'large volumes of gas' stored there" when analyzing the first prong of *Complete Auto*.[3] The courts below erred to place so much emphasis on the owner's identity, leading to needless confusion within Texas jurisprudence.

B. The Eastland Court has collapsed *Complete Auto* down to simply whether goods are "in transit," creating a conflict with this Court's decision in *Diamond Shamrock*.

The only factor the Eastland Court considered when evaluating substantial nexus was the "in transit" status of the oil. *BP America* op. at 9-10. That mechanical reasoning distorts this Court's holding in *Diamond Shamrock* that "the circumstances which make the goods 'in transit' may inform" the *Complete Auto* analysis. *Diamond Shamrock Ref. & Mktg. v. Nueces County Appraisal Dist.*, 876 S.W.2d 298, 302 (Tex. 1994) (emphasis added). That "may inform" language was deliberate. The "in transit" test is not a perfect substitute for the substantial-nexus test of *Complete Auto.*

The reason is plain enough. If substantial nexus only turned on whether goods were "in transit," then the *Complete Auto* framework would collapse into a one-prong test that the state can never win. That's because Texas courts already use whether goods are "in transit" to determine whether interstate commerce (and thus *Complete Auto*) is implicated at all.[4]

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[3] Brief for the United States as Amicus Curiae, *Missouri Gas Energy v. Schmidt*, No. 08-1458, *available at* http://www.justice.gov/osg/briefs/2009/2pet/6invit/2008-1458.pet.ami.inv.pdf, at p. 21; *see also id.* at pp. 13-17.

[4] Treating "in transit" as a gateway to the *Complete Auto* test also matches how the First Court of Appeals decided *Marathon Ashland Petroleum L.L.C. v. Galveston Cent. Appraisal Dist.*, 236 S.W.3d 335 (Tex. App.—Houston [1st Dist.] 2007, no pet.) (putting an out-of-state buyer's name

Walk through that logic in formal terms: Let's represent goods being in transit as proposition "A" being true. And let's represent goods not being in transit as proposition "not A" being true. If "A" is true (i.e., the goods being taxed are "in transit"), then the state tax is subjected to the *Complete Auto* test. That isn't controversial. But under the Eastland Court's reading of the first prong of that test, the taxing authority would then have to show that "not A" was also true (i.e., that these same goods are not "in transit").

This creates a no-win situation— "A" and "not A" cannot both be true. Under the Eastland Court's view of the test, if the goods are in interstate commerce, the state necessarily lacks substantial nexus. That renders *Complete Auto* useless as a way to evaluate taxes on goods in transit, and cannot be what the Supreme Court meant.

The Eastland Court may have been confused by its overreliance on cases construing the quite different Import-Export Clause, which addresses different constitutional concerns.[5] Its blind application of language in those cases to the Dormant Commerce Clause will confuse the jurisprudence.

on a container did not by itself make the goods "in transit" and, accordingly, that the Dormant Commerce Clause was not implicated).

[5] This Court dealt with that clause in the *VICO* case, which involved foreign trade. *Virginia Indonesia Co. v. Harris County Appraisal Dist.*, 910 S.W.2d 905 (Tex. 1995). The Import-Export Clause gives an exclusive role to Congress, while the Dormant Commerce Clause is more flexible because states have their own role in regulating merely interstate commerce.

III. HAVING TWO RELATED PETITIONS WOULD LET THE COURT BETTER CLARIFY THIS RULE THAN ANY SINGLE PETITION IS LIKELY TO PERMIT.

The Court is fortunate to have two related petitions with different facts. This combination plate offers a more satisfying way to announce a rule than any single, later petition is likely to do:

(1) The *Peoples* petition presents a classic case of natural gas "storage" facilities, akin to a warehouse for goods.

(2) The *BP America* petition presents something more akin to a cross-dock for goods, with some of the oil that barely pauses and other oil subjected to "batching," "blending," and "staging" for different purposes and lasting different periods of time. Although the better holding is that the apportionment made here passes *Complete Auto*, this is undoubtedly a closer case than *Peoples*.

(3) And the pipeline amici have injected a third fact pattern to the case: that of a "mere pipeline" that truly winds through the terrain without any added facilities, processing, or storage — akin to a truck hauling goods driving down the highway.[6] These amici have raised doubts about whether taxes even on such pipelines might pass muster under the prevailing view of federal law. If there is any merit to the pipeline amici's position — if there is doubt under *Complete Auto* about whether the oil in unadorned stretches of pipeline can be subject to *ad valorem* tax — then a rehearing to

[6] The brief says that "the same rationale that MCAD is using for taxing the oil in the tank farm" — its reading of *Complete Auto*, the same one adopted by Oklahoma and blessed by the U.S. Solicitor General — "could be used to try to tax oil in the pipelines." Brief of Amicus Curiae Plains Marketing, L.P. and Plains Marketing GP Inc. in Support of Respondents, *Midland Central Appraisal Dist. v. BP America Prod. Co., et al.*, No. 09-0273, at p. 21 (Dec. 17, 2009).

state the rule clearly should allay those fears. By taking this set of petitions, the Court can draw any appropriate distinctions between a "tank farm" like that in Midland from the stretches of pipeline that run into and out of the facility.

Why is it important that the Court take the chance to speak to such a variety of facts at one time? Because, as some Respondents in *BP America* have pointed out:

> Given the overlap in issues, the Oil Companies are concerned about the implications for them if the Court grants review in *Peoples Gas*. A decision by this Court in *Peoples Gas* likely will be touted as addressing all pipeline transportation cases.

Response to Petition for Review, *Midland Central Appraisal Dist. v. BP America Prod. Co., et al.*, No. 09-0273, at p. 14 (Jun. 16, 2009). Given those concerns, the Respondents urged the Court "if the court decides to grant the petition in *Peoples Gas*, it should simultaneously determine the issues raised here." *Id.* at 15.

This pair of linked petitions is likely to be the Court's best vehicle to speak to these questions for some time. The Court should not lightly bypass this chance to resolve significant confusion within Texas jurisprudence, especially one affecting both the underpinning of local government finance and one of the State's traditional industries.

PRAYER

The motions for rehearing should be granted.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that on May 14, 2010, a true and correct copy of this **Amicus Curiae Brief of TASB Legal Assistance Fund** was served by U.S. mail on all appellate counsel of record in this proceeding as listed below.

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APPENDICES

In The
Court of Appeals
Sixth Appellate District of Texas at Texarkana

No. 06-07-00103-CV

THE PEOPLES GAS, LIGHT, AND COKE COMPANY, Appellant

V.

HARRISON CENTRAL APPRAISAL DISTRICT, Appellee

On Appeal from the 71st Judicial District Court
Harrison County, Texas
Trial Court No. 05-0381

Before Morriss, C.J., Carter and Moseley, JJ.
Opinion by Chief Justice Morriss

OPINION

The large amount of natural gas ordinarily stored under Harrison County has great value. The Harrison Central Appraisal District (the District) has acted to assess a large ad valorem tax bill against a portion of that gas—gas allocable to the account of Peoples Gas, Light, and Coke Company (Peoples). From a judgment favoring the District, Peoples appeals.

The gas in question is stored in a large, depleted natural gas field now used as a natural gas storage facility—the North Lansing facility—part of the interstate pipeline system operated by Natural Gas Pipeline Company of America (Pipeline). Peoples is a distribution company that purchases natural gas from suppliers and delivers it to users in Chicago, Illinois. Pipeline, not a party to this matter, operates the interstate pipeline system pursuant to regulations promulgated by the Federal Energy Regulatory Commission (the Commission). Peoples buys natural gas already on the interstate pipeline system owned and operated by Pipeline. Pipeline representatives testifying at trial emphasize that there are many storage facilities associated with its pipeline and that the pipeline is operated "in the aggregate." In other words, Pipeline's storing and transporting gas does not use any particular storage field exclusively.

Pipeline pays ad valorem taxes on what is called "cushion gas" in North Lansing, the significant volume of natural gas that remains in the storage facility and provides the necessary pressure and balance to facilitate the safe, efficient operation of the pipeline. Beginning in 1999, the District allocated to Peoples a portion of the "working" natural gas balance—the volume of gas (above the "cushion") that is transported and delivered to pipeline customers—and assessed taxes on the value of that portion of the natural gas stored at North Lansing. Peoples successfully challenged the assessment and, on advice of its appraisal consultant firm, the District removed Peoples from the tax rolls. The same thing happened in 2000.

For tax years 2003–2005, the District again attempted to assess taxes against Peoples on a portion of the gas stored at North Lansing. This time, on advice from a new consultant firm, the District refused to remove Peoples from the tax rolls. Instead, the District assessed Peoples' portion of the gas at North Lansing, for those years, at values exceeding nine million, forty million, and forty-three million dollars, respectively. Those tax years and tax levies are at issue in this case.

The gas volume figures allocable to Peoples are based on Pipeline's records.[1] Pipeline compares the total contractual balance for all the NSS[2] shippers that have contracts on Pipeline's Gulf Coast Leg to the "working" natural gas balance at North Lansing at the end of the year. This yields a percentage that is multiplied by each shipper's NSS contractual balance on the Gulf Coast Leg of the pipeline at the end of the year to arrive at the allocation it attributes to a customer.

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[1]Pipeline's representative explained that its allocation methods were not for the purpose of determining ownership. It merely did what it was asked to do for the courts to decide the issue of ownership.

[2]Pursuant to Commission tariffs, Pipeline offers several types of contracts to shippers on its pipeline system. Most common are the "NSS" and "DSS" contracts. NSS storage requires a customer such as Peoples to request or nominate a withdrawal to get delivery on a date certain. DSS storage service, on the other hand, allows for no-notice delivery.

The trial court ruled that the District has the authority to assess the ad valorem taxes for the years in question on the gas it allocated to Peoples. We review de novo the trial court's conclusions of law determining each question of law independently. *Quick v. City of Austin*, 7 S.W.3d 109, 116 (Tex. 1999). We review the trial court's findings of fact for legal and factual sufficiency, as we do with jury findings. *See Ashcraft v. Lookadoo*, 952 S.W.2d 907, 910 (Tex. App.—Dallas 1997, pet. denied).

Our analysis leads us, through the following logical steps, to conclude that taxing this gas infringes the Commerce Clause:

(1) Peoples owns this gas for ad valorem tax purposes.
(2) The Commerce Clause shields this gas from ad valorem taxation.
  (A) This gas is in interstate commerce.
  (B) This storage does not remove this gas from interstate commerce.
  (C) The District cannot tax this gas.

For these reasons, we reverse the judgment of the trial court and render judgment that assessing these ad valorem property taxes for these years was improper.

(1) Peoples Owns this Gas for Ad Valorem Tax Purposes

The District and Peoples agree that, under the Commission's regulations, Pipeline does not own the gas in its pipeline system. Peoples contends that it does not own, for ad valorem tax purposes, any amount of the massive volume of natural gas lying beneath Harrison County; the District responds that someone must own the gas, and, since Pipeline certainly does not, Peoples *must* be the taxable owner of the portion of the gas allocable to its account.

"Property taxes are the personal obligation of the person who owns or acquires the property on January 1 of the year for which the tax is imposed." TEX. TAX CODE ANN. § 32.07(a) (Vernon 2008). The Texas Tax Code does not define "own" or "owner" for purposes of assessing ad valorem taxes. Texas courts have generally defined taxable "owner" as the individual or entity holding legal title to the property or holding an equitable right to obtain legal title. *See Childress County v. State*, 127 Tex. 343, 92 S.W.2d 1011, 1015 (1936); *Travis Cent. Appraisal Dist. v. Signature Flight Support Corp.*, 140 S.W.3d 833, 840 (Tex. App.—Austin 2004, no pet.); *Comerica Acceptance Corp. v. Dallas Cent. Appraisal Dist.*, 52 S.W.3d 495, 497 (Tex. App.—Dallas 2001, pet. denied). If an individual or entity does not hold perfect legal title, however, that individual or entity may still be considered the taxable owner of property "if he is the record owner, or is vested with the apparent legal title, or is in possession thereof, coupled with such claims and evidences of ownership as will justify the assumption that he is the owner thereof." *Childress County*, 92 S.W.2d at 1015; *Signature Flight Support Corp.*, 140 S.W.3d at 840. The term "owner" has no fixed legal meaning:

> The meaning of the term owner is not the same under all circumstances. It is not a technical term or word at all, but one of wide application in various connections. In all instances its meaning must be ascertained from the context and subject matter.

Realty Trust Co. v. Craddock, 131 Tex. 88, 112 S.W.2d 440, 443 (1938); *see Signature Flight Support Corp.*, 140 S.W.3d at 839. That said, we examine the "context and subject matter" here to determine whether Peoples owns the gas in question.

We begin with a short explanation of the highly regulated natural gas transportation and storage system and the dealings between Pipeline and its customers, including Peoples. The Commission restructured the natural gas transport and storage industry in 1992. This restructuring created a system of commercial rights for the pipeline customer that was separate from the physical operation of the pipeline system. Buyers and sellers conduct transactions at commercial points—"paper points" or imaginary points—along the pipeline at which a purchase may be completed, points that do not necessarily reflect the physical location of the gas purchased. Pursuant to this restructuring and to facilitate purchase transactions, Pipeline established geographical zones, such as the South Texas zone, the "TEX-OK" zone, and the Iowa-Illinois zone, which help identify the distance the gas is transported from the point at which it was injected into the pipeline system.

Applying the *Comerica/Travis County* test, we conclude Peoples is the owner for ad valorem taxation purposes. As the parties agree, Pipeline has complete control of the physical operation of the pipeline system. Pipeline decides where and when the natural gas is stored. There is no physical connection between a Pipeline customer's storage account balance and physical volumes at any particular storage facility. The District acknowledges that Pipeline's accounting methods are completely divorced from the physical reality of the natural gas location. Pipeline's customers purchase volumes of natural gas at what the parties refer to as a "paper" pooling point after which time, Peoples emphasizes, the purchaser retains no control to direct the physical movement of the natural gas purchased. Peoples also emphasizes that Pipeline's storage fields are operated on an aggregated basis. That is, none of its services are specifically linked to any particular storage field.

Relevant documents show that Peoples purchased natural gas and paid for its transportation to the Iowa-Illinois zone. Of course, the fungible and ethereal nature of natural gas makes it impossible to ascertain the physical location of a given allocated portion of natural gas at any moment. Peoples contends that this documentary evidence in the form of Commission-approved agreements between Peoples and Pipeline suggests that Peoples' allocation of natural gas is "contractually" located in the Iowa-Illinois zone. Obviously, Pipeline cannot identify particular volumes of gas as belonging to a particular customer when physically transporting or storing natural gas.

Consistent with Commission regulations, Pipeline is in full custody, control, and possession of the natural gas within the pipeline system. Only Pipeline can direct the physical movement of the gas once it is placed in the pipeline; and, even after a purchase of gas at a paper pooling point, the purchaser obtains no control over the physical movement of the volume of natural gas purchased. Peoples has no legal right to the natural gas located at North Lansing; it cannot specifically request gas from that facility and could not merely back a truck up to the facility and remove any amount of natural gas. Nor is there any indication that it could do any such thing in Illinois. Peoples emphasizes that it owns merely contractual rights to physically receive natural gas in Chicago and that its purchases from Pipeline call for contractual storage in the Iowa-Illinois zone.

Nonetheless, by regulation, ownership rights could not be transferred to Pipeline. That said, according to the District, legal title must lie with Peoples. No doubt gas is stored beneath Harrison County; there must be an owner of that gas for tax purposes. Considering the nature of the product at issue here, the nature of the pipeline in which customers' fungible goods must be commingled, and the highly regulated industry in which Pipeline and Peoples conduct their business and which prohibits Pipeline from having ownership rights in the gas but requires that it maintain physical control of the natural gas, we conclude the trial court correctly decided that, for tax purposes, Peoples owns an allocation of the natural gas stored in Harrison County.[3]

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[3]Last year, the Kansas Supreme Court decided a case similar to the instant case. *See In the Matter of the Appeal of the Director of Prop. Valuation*, 284 Kan. 592, 161 P.3d 755 (2007). In that case, several non-Kansas entities (municipal utilities, natural gas marketing company, and public utilities) had contracted for gas storage or deferred delivery with an interstate pipeline that maintained storage facilities in Kansas. *Id*. The parties stipulated that none of the entities had facilities within Kansas or sold, traded, or delivered natural gas anywhere in Kansas. *Id.* at 594. In Kansas, a public utility's property is not exempt from ad valorem taxes. The taxing entity argued that non-Kansas companies were public utilities within the following definition: "that own, control, and hold for resale stored natural gas in an underground formation in this state." *Id.* at 597. Based on the legal and contractual relationship between the pipeline and its customers established by Commission-approved tariffs, the Kansas Supreme Court concluded the entities were not public utilities because they did not "control" and "hold for resale" the stored natural gas. *Id.* at 606. With that, the non-Kansas companies' allocations were exempt from ad valorem taxes. It did, however, touch on the ownership aspect of the "public utility" definition:

> There is no serious dispute that the Taxpayers own (or at least hold contractual rights to) storage balances of natural gas contained in underground formations in the state. Nevertheless, whether the Taxpayers actually control and hold the natural gas is doubtful. It is undisputed that tariffs issued by the . . . Commission . . . establish that control and possession of natural gas delivered to interstate pipelines for transportation and storage is vested in the pipelines until the gas is redelivered to their customers. It is also undisputed that the interstate pipelines cannot track and

(2) The Commerce Clause Shields this Gas from Ad Valorem Taxation

Peoples argues that, even if it could be said that it is the taxable owner in this matter, the Commerce Clause shields it from the District's assessment since the natural gas is in interstate commerce and since the tax cannot pass the test that would permit the District to assess such a tax on this property. We agree.

The Commerce Clause grants Congress the power to regulate interstate commerce. U.S. CONST. art. I, § 8, cl. 3. Congress protects interstate business activity by restricting state regulation of interstate commerce.[4] *See Marathon Ashland Petroleum, L.L.C. v. Galveston Cent. Appraisal Dist.*, 236 S.W.3d 335, 337–38 (Tex. App.—Houston [1st Dist.] 2007, no pet.).

(a) This Gas Is in Interstate Commerce

Traditionally, the United States Supreme Court has identified three ways in which goods can enter the stream of interstate commerce: (1) the goods have been shipped, (2) the goods have been placed with a common carrier, or (3) the goods have started a continuous route or journey into

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> account for discrete packages or molecules of natural gas delivered for storage. As the Supreme Court said in *Central Illinois*, under federal regulations the pipeline customers have "little or no control over where the severed natural gas is stored or for how long."

Id. at 603. Our conclusion on the ownership issue is consistent with the Kansas Supreme Court's conclusion.

[4]Congress has granted the Commission exclusive jurisdiction to regulate the natural gas industry through the Natural Gas Act (NGA). *Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293 (1988).

interstate commerce. *See Coe v. Errol*, 116 U.S. 517, 527 (1886); *Marathon Ashland Petroleum, L.L.C.*, 236 S.W.3d at 338. The goods become a part of interstate commerce when their movement demonstrates that the goods have started and are bound for another state. *See Hughes Bros. Timber Co. v. Minnesota*, 272 U.S. 469, 476 (1926). Goods are not a part of interstate commerce when the record shows only preparation or intent to send those goods out of state. *See id.*; *Marathon Ashland Petroleum, L.L.C.*, 236 S.W.3d at 340–41.

Here, it is apparent that the natural gas has been placed with a common carrier, Pipeline. Unlike the taxpayer in *Marathon Ashland Petroleum, L.L.C.*, Peoples does not maintain any control over the physical movement of the gas. Moreover, that common carrier is an interstate pipeline specifically governed by the Commission. There is little dispute that the natural gas in the *pipeline* is in interstate commerce. A critical question is whether the gas in North Lansing storage is similarly in interstate commerce.

(b) This Storage Does Not Remove this Gas from Interstate Commerce

The District takes the position that, although an extremely small portion of the natural gas (that portion actually moving in the pipeline) is actually in interstate commerce, the rest of the natural gas is stored and therefore subject to local taxation wherever it is located. More specifically, the District argues that the fact that the portion of natural gas allocated to Peoples here is not actually moving in the pipeline and is, rather, stored beneath Harrison County takes the gas outside interstate commerce, leaving it subject to taxation as a part of the mass of property within the State of Texas. *See Coe*, 116 U.S at 527; *Marathon Ashland Petroleum, L.L.C.*, 236 S.W.3d at 338.

We conclude this contention fails in the face of two areas of the law: authorities determining the effect of transportation stoppage on whether a product is in interstate commerce and authorities more specifically addressing storage of natural gas.

First, we look to the line of cases examining generally the circumstances surrounding the stoppage of products that have been injected into the stream of interstate commerce and determining whether a stoppage in a jurisdiction would subject the goods to local taxation. *See Indep. Warehouses, Inc. v. Scheele*, 331 U.S. 70, 73 (1947); *see also Virginia Indonesia Co. v. Harris County Appraisal Dist.*, 910 S.W.2d 905, 912–13 (Tex. 1995).[5] When there is a break in the interstate transit, the property may come to rest within a state and become subject to the power of the state to impose a nondiscriminatory property tax. *Indep. Warehouses, Inc.*, 331 at 72–73. The crucial question in determining whether the state may exert its taxing power is whether there is "continuity of transit." *Id.* at 73 (citing *Carson Petroleum Co. v. Vial*, 279 U.S. 95, 101 (1929)). The United States Supreme Court explained the concept:

> If the interstate movement has begun, it may be regarded as continuing, so as to maintain the immunity of the property from state taxation, despite temporary interruptions due to the necessities of the journey or for the purpose of safety and

[5]In *Virginia Indonesia Company*, the Texas Supreme Court determined whether the Import-Export Clause would permit imposition of an ad valorem tax. Similar considerations are involved when determining the "continuity of transit" for purposes of the Commerce Clause. *See* 910 S.W.2d at 912.

> convenience in the course of the movement. . . . Formalities, such as the forms of billing, and mere changes in the method of transportation do not affect the continuity of the transit. The question is always one of substance, and in each case it is necessary to consider the particular occasion or purpose of the interruption during which the tax is sought to be levied. . . .

Id. (quoting *Minnesota v. Blasius*, 290 U.S. 1, 9–10 (1933)). We must look at the facts of each case and will consider the owner's intention, the owner's ability to change destination, the agency or method of transportation, the actual continuity of the journey, and the purpose of the interruption. *See Champlain Realty Co. v. Town of Battleboro*, 260 U.S. 366, 377 (1922).

The character of the shipment in such a case depends on the circumstances, including what the owner has done to prepare for the journey and to carry it out. *Virginia Indonesia Co.*, 910 S.W.2d at 912–13. For instance, when the stoppage of property in interstate commerce is necessary for the safety and convenience of the goods, we do not consider the continuity of transit broken. *Indep. Warehouses, Inc.*, 331 U.S. at 73. On the other hand, if the stoppage is attributable to the business purpose of the owner, then we deem the continuity of transit terminated and the goods are subject to tax in the jurisdiction of the stoppage. *Virginia Indonesia Co.*, 910 S.W.2d at 912. Put another way,

> [w]here property has come to rest within a State, being held there at the pleasure of the owner, for disposal or use, so that he may dispose of it either within the State, or for shipment elsewhere, as his interest dictates, it is deemed to be a part of the general mass of property within the State and is thus subject to its taxing power.

Indep. Warehouses, Inc., 331 U.S. at 73.

In the instant case, the record shows and the law requires that Peoples has no control over the physical operations of the pipeline. Control lies solely with Pipeline. Since Peoples has no control over where that natural gas is stored and how much is stored at any given location, we cannot say that Peoples made the decision to store gas at North Lansing in order to serve its business purpose. Simply put, it made no decision at all regarding the physical location of the stored natural gas.

The District contends Peoples benefits from the storage at North Lansing since it can buy gas at a cheaper rate in the summer months and store it for later use in the winter months when the demand in the Chicago area increases dramatically. It may well be the case that the advent of a pipeline system that will allow for storage of a significant amount of natural gas is beneficial to local distributing companies generally. Indeed, such a system would seem to be beneficial to all. Such a benefit, however, does not alter the fact that Peoples, while benefitting from a storage system generally, makes no decision to store the natural gas at North Lansing specifically. The record shows that the contracts between Peoples and Pipeline do not specify that the gas would be located in Texas. In fact, those agreements provide for "contractual" storage in Iowa and Illinois. The truth is, Pipeline operates its system without regard to the physical reality of identifying a specific storage facility at which any customer's volume of natural gas will be physically stored. Rather, Pipeline operates the pipeline on an "aggregate" basis in which all the storage facilities serve the pipeline as needed to operate efficiently and effectively. With these facts in mind, we conclude that the stoppage of natural gas in North Lansing does not serve the business purpose of Peoples. To the contrary, Peoples has no control over where the natural gas is stored, and we cannot say that the stoppage in Harrison County serves a business purpose as contemplated by the cases dealing with the continuity of transit of goods in interstate commerce.

Second, we examine law specifically concerning the storage of natural gas. Commission regulations provide some guidance as to whether storage would take the natural gas out of the stream of interstate commerce: "Transportation includes storage, exchange, backhaul, displacement, or other methods of transportation." 18 C.F.R. § 284.1(a). By regulation, then, at least some storage is considered a part of the transportation process. Therefore, storage can be a part of *interstate* transportation. Storage in North Lansing, then, as a matter of regulatory definition, would not necessarily take the natural gas out of the stream of interstate commerce.

Indeed, the United States Supreme Court has spoken on this issue:

> Petitioners argued below that Storage was not a natural gas company within the meaning of the NGA, contending that the storage of gas constitutes neither the transportation nor the sale of gas in interstate commerce. Both courts below rejected this argument . . . reasoning that "transportation" includes storage. "Underground gas storage facilities are a necessary and integral part of the operation of piping gas from the area of production to the area of consumption."

Schneidewind, 485 U.S. at 295 n.1 (quoting *Columbia Gas Transmission Corp. v. Exclusive Gas Storage Easement*, 776 F.2d 125, 129 (6th Cir. 1985)); *see also Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157, 166–68 (1954) (evaluating Texas tax on "gathering" gas in context of interstate pipeline, characterizing situation and "so closely related to interstate transportation as to be practically a part of it," and concluding that the tax in that situation violated Commerce Clause). This storage of this natural gas in North Lansing does not take the gas out of interstate commerce. To conclude otherwise would be to segregate, from the pipeline itself, a function deemed "necessary and integral" to the pipeline. We will not do so and, instead, conclude that this storage does not take this natural gas out of the stream of interstate commerce it entered by injection into an interstate pipeline. The natural gas allocated to Peoples is in the stream of interstate commerce, and this storage does not remove it from interstate commerce.

(c) The District Cannot Tax this Gas

It remains possible that the District could still have the authority to tax the portion of natural gas allocated to Peoples, despite the fact that the natural gas has been injected into and remains within the stream of interstate commerce. A state tax does not violate the Commerce Clause if it (1) is applied to an activity with a substantial nexus with the taxing state, (2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly related to the services provided by the state. *See Vinmar v. Harris County Appraisal Dist.*, 947 S.W.2d 554, 555 (Tex. 1997) (citing *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977)); *Diamond Shamrock Ref. and Mktg. Co. v. Nueces County Appraisal. Dist.*, 876 S.W.2d 298 (Tex. 1994); *Rylander v. 3 Beall Bros. 3, Inc.*, 2 S.W.3d 562, 570 (Tex. App.—Austin 1999, pet. denied). If a tax does not satisfy this test, called the *Complete Auto* test, the Commerce Clause prohibits the tax. *See Harris County Appraisal Dist. v. Transamerica Container Leasing, Inc.*, 920 S.W.2d 678, 682 (Tex.

App.—Houston [1st Dist.] 1995, writ denied). The second and third parts of the *Complete Auto* analysis, which require fair apportionment and nondiscrimination, prohibit taxes that pass an unfair share of the tax burden onto interstate commerce. *Quill Corp. v. N.D.*, 504 U.S. 298, 313 (1992). The first and fourth prongs, which require a substantial nexus and a relationship between the tax and state-provided services, limit the reach of state taxing authority so as to ensure that state taxation does not unduly burden interstate commerce. *Id.*

The Commerce Clause requires "some definite link, some minimum connection,[6] between a state and the person, property, or transaction it seeks to tax." *Allied-Signal, Inc. v. Director, Division of Tax*, 504 U.S. 768, 777 (1992) (quoting *Miller Bros. v. Maryland*, 347 U.S. 340, 344–45 (1954)); *3 Beall Bros. 3, Inc.*, 2 S.W.3d at 570. The Commerce Clause requirement of a substantial nexus with the taxing state is satisfied by the taxpayer's physical presence in the state. *3 Beall Bros. 3, Inc.*, 2 S.W.3d at 570; *Lawrence Indus., Inc. v. Sharp*, 890 S.W.2d 886, 892–93 (Tex. App.—Austin 1994, writ denied); *see also Quill Corp.*, 504 U.S. at 312–14.

The record demonstrates that Peoples maintains no office in Texas. Nor does it have any employees, representatives, or physical facilities in the State. The physical facilities in Harrison

[6]The "substantial nexus" requirement is not, like due process' "minimum contacts" requirement, a proxy for notice, but rather a means for limiting state burdens on interstate commerce. *Quill Corp.*, 504 U.S. at 313. Accordingly, an entity may have the "minimum contacts" with a taxing state as required by the Due Process Clause, and yet lack the "substantial nexus" with that state as required by the Commerce Clause. *Id.*

County belong to Pipeline, as does the decision to use the North Lansing facility. Further, there is no evidence that any of the natural gas Peoples has purchased is delivered to any customer in Texas.

If we were to look strictly at the generic act of storing gas in a reservoir in Harrison County, it might appear that such an activity would have a substantial nexus with the State. We note again that, as required by the Commission regulations, Pipeline—not Peoples—directs that activity, and we are to consider not whether Pipeline's activities have a substantial nexus with the State, but whether Peoples' activities do. Peoples engages in the purchase and delivery of natural gas to its customers in Chicago. Its only connection in this respect to Texas is through the structure and location of Pipeline's pipeline and Pipeline's decision to store a significant amount of natural gas in North Lansing. Such a connection is too tenuous to subject Peoples to ad valorem taxation in Texas.[7]

The District contends the nexus lies between the natural gas and the State. The natural gas, it argues, comes from Texas and is, thus, substantially connected to the State such that the State should be allowed to tax it. The record suggests that much of the gas is Texas-produced.

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[7]We also note our sister court's opinion in *Rylander v. Bandag Licensing Corp.*, 18 S.W.3d 296 (Tex. App.—Austin 2000, pet. denied). In *Bandag Licensing Corp.*, the Austin court suggests that "when the corporation conducts its activity solely through interstate commerce and lacks any physical presence in the state, no sufficient nexus exists to permit the state to assess tax." *Id.* at 300. That connection, along with the facts that the corporation's only activity was the "passive possession of a license to do business in Texas" and that the corporation had no physical presence in Texas, led the court to conclude that the Commerce Clause prohibited the imposition of a state tax in that situation.

Nevertheless, we do not have specific volumes of that production, nor could we ever know the location from which Peoples' allocation originated.

We conclude that, despite the fact that Peoples owns some of the natural gas on the system and thus under Harrison County, the storage of natural gas at the North Lansing field is an insufficient nexus when we consider the particular, unique circumstances at hand and the complex relationships among the parties involved. We find insufficient nexus between Texas and the entity, property, or transaction to be taxed. That said, the District's tax fails to satisfy the first prong of the *Complete Auto* test and, therefore, violates the Commerce Clause.

Moving to other parts of the test, we look at the relation between Peoples and services provided in Harrison County. Under the Commerce Clause, the measure of the tax must be reasonably related to the extent of the taxpayer's presence or activities within the taxing state and to the taxpayer's consequent enjoyment of the opportunities which the state has afforded. *3 Beall Bros. 3, Inc.*, 2 S.W.3d at 571. Even though fire and police services may not be invoked, protection conferred by these "along with the usual and usually forgotten advantages conferred by the state's maintenance of a civilized society are justifications enough for the imposition of a tax." *See Transamerica Container*, 920 S.W.2d at 683. The District presented substantial evidence of services provided within the county. While we do not doubt the value of those services, we note, again, that services such as law enforcement and the fire department would serve the North Lansing facility itself, and the facility undoubtedly belongs to Pipeline, which does pay ad valorem taxes on both the "cushion" gas it maintains in the facility and the physical plant of the facility itself.

Having found that the District's tax on Peoples' gas fails to meet, at least, the first and fourth prongs of the *Complete Auto* test, we conclude that assessment of ad valorem taxes, on these facts, runs afoul of the Commerce Clause.

We reverse the trial court's judgment and render judgment that assessing these ad valorem property taxes for these years is improper.

Josh R. Morriss, III
Chief Justice

Date Submitted: June 18, 2008
Date Decided: September 24, 2008

Opinion filed March 26, 2009

In The

Eleventh Court of Appeals

No. 11-07-00048-CV

MIDLAND CENTRAL APPRAISAL DISTRICT, Appellant/Cross-Appellee

V.

BP AMERICA PRODUCTION COMPANY ET AL, Appellees/Cross-Appellants

On Appeal from the 238th District Court

Midland County, Texas

Trial Court Cause No. CV44864 (consolidated)

O P I N I O N

The issue in this case is whether an ad valorem tax may be imposed on crude oil located in Midland County in a tank farm that is an integral part of an interstate, common carrier pipeline system. In its appraisal rolls for 2003 and 2004, Midland Central Appraisal District (MCAD) included oil located in the tank farm on January 1 of the respective years. MCAD allocated ownership of the oil to various shippers, including BP America Production Company; Amerada Hess Trading Company; Chevron USA, Inc.; ChevronTexaco Products Company; ChevronTexaco Global

Supply and Trading Company; TEPPCO Crude Oil LLC; and TEPPCO Crude P/L LLC (hereinafter referred to collectively as the Oil Companies). The Oil Companies properly protested and ultimately brought four separate suits in district court. After consolidating the suits and conducting a nonjury trial, the trial court rendered judgment that the oil was not taxable but denied the Oil Companies' request for attorney's fees. MCAD appeals the trial court's ruling regarding the taxability of the oil, and the Oil Companies appeal the denial of attorney's fees. We affirm.

I. *Issues*

MCAD presents six issues for review. In the first issue, MCAD contends that the trial court erred as a matter of law in determining that the oil is not taxable in Midland County. In the second issue, MCAD contends that the trial court erred in finding that oil had no situs in Midland County. In the third issue, MCAD contends that the trial court erred in holding that the oil was in interstate commerce. In its fourth issue, MCAD challenges the legal and factual sufficiency of several findings of fact and asserts that the trial court erred in considering the oil as individual barrels rather than an aggregate inventory. MCAD argues in its fifth issue that the trial court erred in finding that the tax is not applied to an activity or oil with a substantial nexus to Texas. In its final issue, MCAD asserts that the trial court erred in finding that MCAD's allocation of ownership of the oil was not reasonable.

The Oil Companies present two issues for review. In their first issue, the Oil Companies contend that the trial court erred in denying their request for attorney's fees because the award of attorney's fees was mandated by statute, specifically TEX. TAX CODE ANN. § 42.29 (Vernon 2008). In their second issue, the Oil Companies assert that MCAD waived its challenge to the award of attorney's fees by requesting findings of fact that support the award.

II. *Background Facts*

The record shows that the underlying facts in this case are largely undisputed. The unchallenged findings of fact indicate that oil at issue in this case was produced mostly in West Texas and a small amount in eastern New Mexico and was injected into the Midland Pipeline System, a spiderweb configuration of interconnecting pipelines covering more than two dozen counties in West Texas and eastern New Mexico. The Midland Pipeline System is an interstate, common carrier pipeline system that is regulated by the Federal Energy Regulatory Commission and is operated by various pipeline companies that are not parties to these proceedings. Upon injection of the subject oil into a pipeline, control and custody was relinquished to the pipeline companies; the oil, being fungible, became part of the common stream of oil.

Oil in the system travels through pipelines in Texas, taking no more than two and one-half weeks, to final destinations at various oil refineries located in Texas and in other states. During the journey, a large amount of oil passes through the tank farm where the Midland Pipeline System converges. The tank farm functions as an integral part of the Midland Pipeline System and exists to facilitate the transportation of the oil, not to store oil. The oil in the tank farm arrives and exits via the Midland Pipeline System. The time from entry into a tank to exit from a tank is six to seventy-two hours. However, a certain minimum volume of cushion oil is required to be maintained in each tank for safety reasons and to meet emission standards, resulting in the constant presence of a large amount of oil in the tank farm. Blending, batching, or staging of the oil may occur at the tank farm as necessary to facilitate the transmission of the oil through the Midland Pipeline System, but these processes do not interrupt the continuity of transit. The tanks are not used for storage.

Oil is bought, sold, and traded by document transfers irrespective of where the oil may be in the system. These transfers do not alter the movement of the oil or interrupt its in-transit movement to refineries. Upon arrival at a refinery, the oil is assessed and listed for taxation by the local appraisal authorities.[1] Furthermore, ad valorem taxes are assessed on the pipelines, tanks, physical assets, and equipment at the tank farm. In 2003 and 2004, those ad valorem taxes were timely paid.

III. *MCAD's Appeal*

A. Sufficiency of the Challenged Findings.

MCAD challenges several of the trial court's findings regarding the temporariness of the oil in Midland County and in Texas, the continuity of the oil's transit, the ultimate destination of the oil, and the oil's status as being in interstate commerce. MCAD argues in its fourth issue that there is no evidence to support the challenged findings and that the evidence is factually insufficient to support those findings. MCAD also argues in its fourth issue that the trial court erred in considering the oil as individual barrels of oil rather than an oil inventory.

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[1]We note also that a production tax is levied on oil that is produced in Texas. TEX. TAX CODE ANN. § 202.051 (Vernon 2008).

We review sufficiency challenges to a trial court's findings of fact under the same standards that we use to review a jury's findings. *Catalina v. Blasdel*, 881 S.W.2d 295, 297 (Tex. 1994); *Anderson v. City of Seven Points*, 806 S.W.2d 791, 794 (Tex. 1991). In analyzing a legal sufficiency challenge, we must determine whether the evidence at trial would enable reasonable and fair-minded people to reach the verdict under review. *City of Keller v. Wilson*, 168 S.W.3d 802, 827 (Tex. 2005). We must review the evidence in the light most favorable to the challenged finding, crediting any favorable evidence if a reasonable factfinder could and disregarding any contrary evidence unless a reasonable factfinder could not. *Id.* at 821-22, 827. We may sustain a no-evidence or legal sufficiency challenge only when (1) the record discloses a complete absence of a vital fact, (2) the court is barred by rules of law or evidence from giving weight to the only evidence offered to prove a vital fact, (3) the only evidence offered to prove a vital fact is no more than a mere scintilla, or (4) the evidence conclusively establishes the opposite of a vital fact. *Id.* at 810 (citing Robert W. Calvert, *"No Evidence" and "Insufficient Evidence" Points of Error*, 38 TEX. L. REV. 361, 362-63 (1960)). In analyzing a factual sufficiency challenge, we must consider and weigh all of the evidence and determine whether the evidence in support of a finding is so weak as to be clearly wrong and unjust or whether the finding is so against the great weight and preponderance of the evidence as to be clearly wrong and manifestly unjust. *Dow Chem. Co. v. Francis*, 46 S.W.3d 237, 242 (Tex. 2001); *Pool v. Ford Motor Co.*, 715 S.W.2d 629, 635 (Tex. 1986); *In re King's Estate*, 244 S.W.2d 660, 661 (Tex. 1951). We review a trial court's conclusions of law, including those mislabeled as findings of fact, de novo. *See BMC Software Belgium, N.V. v. Marchand*, 83 S.W.3d 789, 794 (Tex. 2002).

At trial, several witnesses, including employees of the pipeline companies, explained that a tank is basically a wide spot in a pipeline and that the tank farm is simply a gathering location of multiple pipelines that bring barrels of oil in at varying rates and varying pressures and allows the oil to be gathered to move on to the next destination. The Oil Companies are not allowed to store oil in the pipeline system. The oil in the tanks is in constant movement: either filling or withdrawing. After reviewing all the evidence, we hold that, although there is a substantial quantity of oil that is constantly present in the tanks, the trial court's findings regarding the continuity of the oil's transit are supported by legally and factually sufficient evidence.

MCAD also challenges findings regarding the ultimate destination of the oil and the oil's status as being in the stream of interstate commerce. The trial court found that a vast majority of the oil located in the tank farm is sent to refineries located outside of Texas and that less than ten percent of the oil remains in Texas. These findings are supported by testimony showing that the oil passing through the tank farm travels through the pipeline system and can be offloaded at only three refineries in Texas. Testimony showed that the amount of oil offloaded at these three refineries amounts to less than ten percent of the oil that passes through the tank farm in the pipeline system and that "the rest of the oil has to leave the state." After reviewing all of the evidence, we hold that the challenged findings of fact are supported by legally and factually sufficient evidence. To the extent that MCAD's fourth issue challenges the sufficiency of the evidence, it is overruled.

B. Was the Oil Taxable in Midland County?

Unless exempt by law, tangible personal property in Texas is taxable if it is located in Texas for longer than a temporary period, is temporarily located outside Texas but the owner resides in Texas, or is used continually in Texas. TEX. TAX CODE ANN. § 11.01 (Vernon 2008); *see also* TEX. TAX CODE ANN. § 21.02 (Vernon 2008) (taxable situs in taxing unit). In determining whether the oil at issue in this case was taxable, we address whether the oil was in the stream of interstate commerce, whether the trial court erred in failing to consider the oil as a constant presence in the tanks rather than individual barrels in transit, and whether the oil had situs in Midland County. We ultimately conclude that the tax violated the Commerce Clause of the United States Constitution, U.S. CONST. art. I, § 8, cl. 3, and that the tax was not valid under Section 21.02(a)(1) due to the temporary period during which the oil was located in Midland County.

1. Interstate Commerce.

The first question is whether the oil had been placed into the stream of interstate commerce. MCAD argues that it had not. Interstate commerce "occurs when goods 'have been shipped, or entered with a common carrier for transportation to another State, or have been started upon such transportation in a continuous route or journey.'" *Va. Indon. Co. v. Harris County Appraisal Dist.*, 910 S.W.2d 905, 908 (Tex. 1995) (*VICO*) (citing *Coe v. Errol*, 116 U.S. 517, 527 (1886)).

The trial court found and the uncontroverted evidence indicates that, prior to making its way to the tank farm, the subject oil was injected into a federally regulated, interstate common carrier pipeline system. Once injected, the oil remained in the pipeline and under the pipeline's control until it reached its ultimate destination, a refinery. The evidence also shows that the tanks in the tank farm are and were an integral part of the interstate pipeline system and that, although the destination of the oil actually in the tanks at the time of the assessment could not be determined, over ninety percent of the oil passing through the tank farm was transported to refineries out of state. *See Eureka Pipe Line Co. v. Hallanan*, 257 U.S. 265, 272 (1921) (stating that a tank in an oil pipeline "may be regarded as a pipe of larger size").

The next question is whether the oil remained in transit in the stream of interstate commerce when it was at the tank farm. MCAD asserts that the subject oil should be viewed as a massive constant presence of oil in the tank farm and that, if so viewed, it cannot be concluded that the oil was in interstate commerce or that it was only temporarily in Midland County. In support of this contention, MCAD relies upon *Diamond Shamrock Refining and Marketing Co. v. Nueces County Appraisal District*, 876 S.W.2d 298 (Tex. 1994), and *Exxon Corp. v. San Patricio County Appraisal District*, 822 S.W.2d 269 (Tex. App.—Corpus Christi 1991, writ denied). We find these cases to be factually distinguishable.

In *Diamond Shamrock*, the supreme court held that oil stored in tanks was subject to an ad valorem tax where the oil was imported from abroad into Texas, which was its final destination. 876 S.W.2d 298. Upon arriving in Texas, the oil, which was owned by Diamond Shamrock and destined for Diamond Shamrock's refinery in Texas, was offloaded into a storage facility and stored in tanks before being transported to a refinery in another county by pipeline. Although the parties stipulated that the oil at issue was "in transit," the court determined that the situs of each barrel should not be considered because the incidence of the tax imposed was the year-round presence in the storage facility of a large volume of oil belonging to Diamond Shamrock. *Id.* at 300-04. The court in *Diamond Shamrock* specifically limited its holding to foreign goods in transit through only one state that remain in that state. *Id.* at 302, n.7. Furthermore, the oil at issue in *Diamond Shamrock* was located in a storage facility, whereas the oil at issue in this case had been injected into interstate common carrier pipelines and was located in tanks that were an integral part of the common carrier pipeline system within the stream of interstate commerce. Even when viewed as a constant presence, the oil at issue in this case, like the massive quantity of oil constantly present within the pipelines themselves, was located in the stream of interstate commerce where it had been commingled with oil from numerous other shippers and was – for the most part – being transported to another state.

In *Exxon*, as in the present case, oil that was located in working tanks was taxed. 822 S.W.2d 269. The court ruled that, although each individual barrel remained in the county for no longer than seventeen days, the oil acquired situs there because Exxon maintained at all times a massive quantity of oil in the tanks. *Id.* at 272-74. As in *Diamond Shamrock*, however, the oil in *Exxon* was not destined for any location outside the State of Texas. The oil at issue in *Exxon* was transported, refined, and sold in Texas. *Id.* at 272. Nothing in the court's opinion in *Exxon* indicates that interstate commerce was involved.

Subsequent to its opinion in *Diamond Shamrock*, the Texas Supreme Court considered and struck down an ad valorem tax assessed on goods that had been placed into the export stream of commerce but were temporarily located in a facility belonging to an independent export packer. *VICO*, 910 S.W.2d at 906-08. Although the court in *VICO* relied upon the Import-Export Clause, U.S. CONST. art. I, § 10, rather than the Commerce Clause to invalidate the tax, the court recognized that the doctrine used to determine whether goods are in transit at the time of taxation applies equally under either clause. *Id.* at 908 & n.1. The court recognized the year-round presence in the packer's facility of goods belonging to VICO but did not rely on the goods' constant presence as a factor in its determination that the goods remained in transit and in the stream of export. *Id.* at 907-14.

In *VICO*, the goods had been committed to foreign export and were transported to the packer's facility to be checked, approved for import into Indonesia, inspected, packaged, and cleared for shipping. *Id.* at 907, 913-14. The court held that the temporary stoppage of the goods at the packer's facility, which usually took no more than forty-five days, did not break the continuity of transit and that the goods remained in the stream of export. *Id.* at 907, 912-14. In determining whether the stoppage disrupted the continuity of transit, the court in *VICO* followed Supreme Court precedent and reasoned that it "is the *purpose* of the stoppage that is important." *Id.* at 912 (citing *Champlain Realty Co. v. Town of Brattleboro*, 260 U.S. 366, 376-77 (1922), and *Minnesota v. Blasius*, 290 U.S. 1, 11-12 (1933)). When the stoppage is attributable to a business purpose of the owner, the in-transit status is deemed to have terminated, and the goods are subject to taxation in the jurisdiction where they are stopped. *Id.* In contrast, if the stoppage is a necessity of the journey or for the purpose of safety and convenience in the course of the journey, the stoppage does not interrupt the continuity of transit. *Id.*

In the present case, the "stoppage" was not related to a business purpose of the owner. The evidence and the trial court's findings indicate that, barring any malfunction, oil is delayed for six to seventy-two hours in the tank farm for purposes related to the operation of the pipeline system. Each tank is required to maintain 8,000 to 10,000 barrels of oil as a cushion for safety and emission reasons. Oil may also be delayed for blending, batching, or staging – operational functions of the pipeline system that are necessary to facilitate the transmission of the oil.[2] Thus, as in *VICO*, the "stoppage" of the oil did not interrupt the continuity of transit.

We hold that the trial court correctly determined that the oil was in the stream of interstate commerce. The oil had been injected into a common carrier pipeline system and remained in that interstate system at the time of the tax assessment. Any delay at the tank farm was not attributable to the Oil Companies but, rather, was incidental to the transportation of the oil by the common carrier and was necessary for the safe and efficient operation of the pipeline system.

2. Validity of Tax Under Commerce Clause.

Next, we must determine whether the tax on the oil in interstate transit violated the Commerce Clause. The Commerce Clause grants Congress the power to regulate interstate commerce and implicitly prohibits certain state regulation of interstate commercial activity. *Okla. Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175 (1995). However, not all state taxes on interstate commerce are prohibited. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Pursuant to *Complete Auto*, a state tax does not violate the Commerce Clause if it meets a four-pronged test set out by the Court. To be valid, the tax must (1) apply to an activity with a substantial nexus with the taxing state, (2) be fairly apportioned, (3) not discriminate against interstate commerce, and (4) be fairly related to the services provided by the state. *Id.* at 279, 287; *Vinmar, Inc. v. Harris County Appraisal Dist.*, 947 S.W.2d 554, 555 (Tex. 1997). To establish that a state tax is unconstitutional,

[2]Blending is the mixing of oil of low sulfur content (sweet crude) with oil of higher sulfur content (sour crude). Batching keeps oil of different grades separate. Staging is the accumulation of sufficient volumes of oil necessary for transmission in the pipeline system.

the taxpayer need only prove that the tax fails one prong of the *Complete Auto* test. *Vinmar*, 947 S.W.2d at 555.

The trial court concluded that the tax violated the Commerce Clause and that the tax did not satisfy the "substantial nexus" requirement of the *Complete Auto* test. The substantial nexus requirement of *Complete Auto* is a means for limiting state burdens on interstate commerce. *Quill Corp. v. North Dakota*, 504 U.S. 298, 313 (1992).

In support of their contention regarding substantial nexus, the Oil Companies cite to a recent opinion of the Texarkana Court of Appeals, *Peoples Gas, Light, & Coke Co. v. Harrison Central Appraisal District*, 270 S.W.3d 208 (Tex. App.—Texarkana 2008, pets. filed). In *Peoples*, the court struck down an ad valorem tax assessed against the owner of natural gas on gas that had been placed into the stream of interstate commerce and was located in an underground storage facility owned by an interstate pipeline company. The court determined that the tax violated the Commerce Clause because the gas owner's activities in Texas and its connection to Texas were too tenuous to create a substantial nexus. 270 S.W.3d at 218.

In contrast, MCAD asserts that we should not follow *Peoples* but should instead follow the decision reached by the Supreme Court of Oklahoma in *In re Assessment of Personal Property Taxes Against Missouri Gas Energy, a Division of Southern Union Co.*, No. 103,355, 2008 WL 4648330 (Okla. Oct. 21, 2008). In *Missouri Gas*, the court upheld an ad valorem tax on gas held in an underground storage facility owned and operated by an interstate, common carrier pipeline. Missouri Gas Energy owned the gas, which was ultimately transported out of state. The Oklahoma court determined that the gas was not merely passing through the county to an out-of-state destination because the large volumes of gas that were stored in the facility for a substantial part of the year were "not in transit in such a way as to invoke the protection of the Commerce Clause." 2008 WL 4648330, at *11.

We find at least one crucial fact of *Missouri Gas* to be distinguishable from the facts of the present case. The crude oil in the present case was not in storage but, rather, was in transit in the stream of interstate commerce. For this same reason, the case at hand presents an even stronger case for a Commerce Clause violation than did the circumstances in *Peoples*.

To comply with the first prong of the *Complete Auto* test, the ad valorem tax on the oil in the tank farm must have applied to an activity with a substantial nexus with Texas. Although the oil itself had a substantial nexus with this state as much of it was produced in this state and some of it was destined for an in-state refinery, the "activity" being taxed had no such nexus. The activity essentially being taxed in this case was the ownership of oil that was present but in transit on January 1 in a tank farm that constituted an integral part of an interstate, common carrier pipeline system.

Furthermore, if the tax in this case is upheld, then ad valorem taxes could potentially be levied by any taxing authority on oil in transit but located, at the time of assessment, in the portion of an interstate pipeline system within the boundaries of that taxing authority. The result would be an impermissible multiple burden on interstate commerce. *See Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157, 170 (1954) (holding that tax on taking of gas into interstate pipeline infringed upon the Commerce Clause and recognizing that such tax would permit a multiple burden upon commerce because other states could impose a tax on the first taking of the same gas in their state). We hold that the tax in the present case does not satisfy the *Complete Auto* test and that it runs afoul of the Commerce Clause.

3. Validity of Tax Pursuant to State Law.

Section 21.02 provides in relevant part that tangible property in Texas is taxable by a taxing unit if "it is located in the unit on January 1 for more than a temporary period." Section 21.02(a)(1).[3] The trial court concluded that the oil was not located in Midland County for longer than a temporary period. We agree.

As discussed above, the record shows that the oil had been injected into an interstate, common carrier pipeline system; that the oil merely traveled through Midland County in the pipeline system; that any delay of the oil in the tank farm was temporary and was necessary only to facilitate the continued transportation of the oil; and that the tank farm was not used for storage. Although

[3]We note that MCAD asserts in its brief that the oil is also taxable pursuant to Section 21.02(a)(4), which allows personal property to be taxed if "the owner resides (for property not used for business purposes) or maintains the owner's principal place of business in this state (for property used for business purposes) in the unit and the property is taxable in this state but does not have a taxable situs pursuant to Subdivisions (1) through (3) of this subsection." However, the trial court made no findings of fact on this issue, and MCAD did not request that the trial court make a finding regarding the principal place of business. Moreover, the evidence does not indicate that Midland County is the principal place of business in this state for any of the Oil Companies.

much of the oil had a nexus with Texas in that it was produced in Texas, it had no such nexus with Midland County. The oil was merely transported through Midland County and was only temporarily located in the county. Thus, we hold that the trial court did not err in concluding that the oil had no taxable situs in Midland County.

The tax was not valid under the Commerce Clause or Section 21.02(a)(1). Consequently, MCAD's first, second, third, fourth, and fifth issues are overruled. We need not reach MCAD's sixth issue concerning allocation of ownership. TEX. R. APP. P. 47.1.

IV. *Oil Companies' Appeal*

The Oil Companies appeal the trial court's refusal to award them attorney's fees. In Texas, attorney's fees are recoverable from an opposing party only when authorized by statute or by contract between the parties. *Travelers Indem. Co. of Conn. v. Mayfield*, 923 S.W.2d 590, 593 (Tex. 1996). The Oil Companies assert that attorney's fees were authorized by Section 42.29 of the Tax Code. The trial court entered findings of fact as to the amount of attorney's fees that would be reasonable if recoverable under Section 42.29. The trial court concluded, however, that the Oil Companies were not entitled to attorney's fees under Section 42.29.

Section 42.29 provides that a "property owner who prevails in an appeal to the court under Section 42.25 or 42.26 may be awarded reasonable attorney's fees." TEX. TAX CODE ANN. § 42.25 (Vernon 2008) provides a remedy for an excessive appraisal, entitling the owner to a reduction of the appraised value on the appraisal roll. TEX. TAX CODE ANN. § 42.26 (Vernon 2008) provides a remedy for the unequal appraisal of property in relation to the appraised values of other properties. Sections 42.25 and 42.26 do not apply to this case because the Oil Companies did not challenge the appraised value of the oil; they challenged the ability of Midland County to tax the oil. Consequently, since the Oil Companies did not prevail on a claim "under Section 42.25 or 42.26," attorney's fees were not authorized by Section 42.29. If the legislature had intended for attorney's fees to be recoverable in a case of this type, it could have included in its Section 42.29 authorization of attorney's fees an appeal challenging the inclusion of the property on the appraisal roll, the determination of ownership, or the denial of an exemption. The legislature specifically authorized such protests in TEX. TAX CODE ANN. § 41.41(a) (Vernon 2008) (listing nine distinct actions that may be protested by taxpayer, including: excessive value, unequal appraisal, denial of an exemption, ownership, and inclusion on tax roll). The legislature, however, did not authorize attorney's fees for all such protests. Section 42.29 authorizes attorney's fees for only two distinct types of protest: excessive value and unequal appraisal. *Dallas Cent. Appraisal Dist. v. Seven Inv. Co.*, 835 S.W.2d 75, 77-79 (Tex. 1992). The Oil Companies' protest cannot be categorized as falling within either of those two. *See id.* The Oil Companies' first issue is overruled.

In the second issue, the Oil Companies assert that MCAD waived any complaint it had to the award of attorney's fees by requesting findings of fact that supported an award of attorney's fees. We disagree. MCAD repeatedly objected to issues related to the prospective award of attorney's fees, and MCAD did not request any findings of fact that would entitle the Oil Companies to attorney's fees or waive MCAD's objection to such fees. MCAD merely requested that the trial court amend its findings regarding attorney's fees to omit the phrase "recoverable under Tax Code § 42.29." The requested amendments reflected MCAD's continued objection to the award of attorney's fees and continued contention that the fees were not "recoverable." Moreover, MCAD did not ask the trial court to amend Conclusion of Law No. 9, wherein the trial court concluded: "The Oil Companies are not entitled to attorney's fees under Tax Code § 42.29." MCAD did not waive its complaint to the award of attorney's fees. The Oil Companies' second issue is overruled.

V. *Conclusion*

The judgment of the trial court is affirmed.

JIM R. WRIGHT
CHIEF JUSTICE

March 26, 2009

Panel consists of: Wright, C.J.,
McCall, J., and Strange, J.