18-BCD-12

IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

SWN PRODUCTION COMPANY, LLC,

Petitioner,

vs.

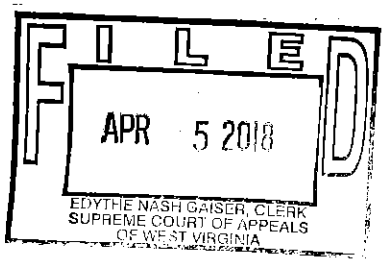
Marshall County Circuit Court
Civil Action No. 18-C-8
The Honorable Judge Cramer

THE HONORABLE DALE STEAGER,
West Virginia State Tax Commissioner,

THE HONORABLE CHRISTOPHER J. KESSLER,
Assessor of Marshall County, and

THE COUNTY COMMISSION OF MARSHALL COUNTY,
Sitting as a Board of Assessment Appeals,

Respondents.



TO: THE HONORABLE CHIEF JUSTICE

MOTION TO REFER CASE TO THE BUSINESS COURT DIVISION

Pursuant to Rule 29.06 of the West Virginia Trial Court Rules, the Petitioner, SWN Production Company, LLC ("SWN"), by counsel, John Meadows, Craig Griffith, and the law firm of Steptoe & Johnson, PLLC, respectfully requests the above-styled case be referred to the Business Court Division for all further proceedings. Trial Court Rule 29.04 expressly provides that "complex tax appeals are eligible to be referred to the Business Court Division." W. Va. Trial Ct. R. 29.04. This matter constitutes a complex tax appeal, and involves issues for which specialized treatment will be helpful. For these reasons, the Court should grant SWN's Motion to Refer Case to Business Court Division.

Additionally, the following related actions should be the subject of consolidation and transferred to the Business Court Division, and are currently pending:

- *SWN Production Company, v. The Honorable Dale Steager, et al.*, Civil Action Number 17-C-319, Ohio County Circuit Court (Judge James P. Mazzone).

- *SWN Production Company, v. The Honorable Dale Steager, et al.*, Civil Action Number 18-C-21, Wetzel County Circuit Court (Judge Cramer).

The above-styled cases present identical claims and issues of law as those in this case. For tax year 2017, SWN appealed the West Virginia Department of Revenue, State Tax Department, Property Tax Division's assessment of its wells in Ohio, Marshall and Wetzel Counties. In the interest of judicial economy, these cases should be consolidated and heard by the Business Court Division. If these cases are not consolidated, two different circuit courts and two different judges will have to hear and decide the same issue, possibly reaching inconsistent results. Thus, not only is this precisely the type of case suited to the Business Court Division, but, here, granting the Motion to Refer will also accomplish the important goal of judicial economy and consistency.

I. INTRODUCTION AND BACKGROUND

SWN is a producer of natural gas throughout the state of West Virginia, with 56 Marcellus wells located in Marshall County. Those wells are appraised by the West Virginia Department of Revenue, State Tax Department, Property Tax Division (the "Tax Department" or "State") based on a mass appraisal system, state-wide. SWN filed this action, as well as actions in Ohio and Wetzel Counties, because the Tax Department failed to properly calculate the fair market value of its Marcellus wells for tax year 2017.

Certain variables are used by the State to value producing oil and natural gas wells, including, operating expenses. Specifically, the Tax Department periodically circulates a survey

by which it solicits data from oil and natural gas producing taxpayers regarding operating expenses for their wells, and based on that, the Tax Department determines the operating expense variables used in its mass appraisal system. The amount of operating expenses applied to a well using the mass appraisal system is based on a percentage of the well's gross receipts not to exceed a maximum amount, and the percentage and maximum vary by the type of well (typical or conventional, Marcellus, etc.). The operating expense calculations are included in a natural resources "valuation variables" document that the Tax Department releases annually.

In addition to the valuation variables document, the Tax Department releases an annual administrative notice that lists the percentages and maximum amounts for operating expense calculations. In prior years, the Tax Department invited taxpayers to submit actual operating expenses that exceed the percentages and maximum amounts listed in the valuation variables document. The 2016 and 2017 administrative notices, unlike administrative notices from 2000 through 2015, however, did not include language that invites taxpayers to submit actual expenses, despite no changes to the West Virginia Code or the Tax Department's Legislative Rule that governs the valuation of producing natural gas wells.

For tax year 2017, the Tax Department calculates operating expenses at the lesser of 20% of gross receipts or $175,000 for Marcellus wells (the "maximum amount" of $175,000 of operating expenses per Marcellus well will be referred to as the "maximum amount" or "cap"). This cap unduly restricts the amount of operating expenses that should be allowed for each well, and the imposition of a "cap" is not supported by the Tax Department's legislative rule regarding the valuation of producing oil and natural gas properties. The legislative rule, instead, requires that the Tax Department use "average annual industry operating expenses per well" in valuing

producing wells, and does not authorize the Tax Department to "cap" operating expenses at a certain amount.

Additionally, the Tax Department overvalued SWN's Marshall County wells by employing a "weighting" methodology for wells that produced both oil and natural gas that significantly decreased the amount of operating expenses that were allowed for the entire well, rather than applying the operating expenses allowed for the oil production and the operating expenses allowed for the gas production separately. This weighting methodology also factored into the Tax Department's overvaluation of SWN's wells, leading to the wells not being assessed at their true and actual value.

In this matter, SWN evaluated its actual operating expenses for calendar year 2015,[1] and determined that for Marcellus wells in the county, the amount of operating expenses that it was incurring significantly exceeded the percentages and maximum amounts set by the State.

SWN, like many mineral producers, generally reports its operating expenses to the Tax Department on a state-wide basis. For calendar year 2015, SWN's average operating expense per well was 56.4% of revenue, or $765,283, which includes all operating expenses, gathering, compression and transportation expenses and processing expenses necessary to get the gas to the point of sale. SWN reports its gross receipts based on the point of sale, and the allowed operating expenses should reflect the expenses incurred to get the gas to the point of sale. The goal of the State's calculation is to determine the value of the reserves. Under the current system, if two producers have the same production/reserves but one sells at the wellhead and the other sells to a market further away, the reserves of the producer who sells to a further market are valued substantially higher, which undermines the goal of the State's calculation. In sum, the

[1] For property tax purposes, the operating expense data from calendar year 2015 is used to value the wells for tax year 2017.

Tax Department incorrectly and unfairly ignored the actual operating expenses and instead relied on the maximum calculations found in its valuation variables document and administrative notice. By failing to consider SWN's actual operating expenses, the Tax Department overvalued SWN's wells and did not assess them at their true and actual value.

On October 5, 2017, SWN protested the Tax Department's valuation (as adopted by the Marshall County Assessor) to the Marshall County Commission sitting as the Marshall County Board of Assessment Appeals (the "Board"). (Certified Transcript of October 5, 2017 Hearing before the Board, See Exhibit A to SWN's Petition, (hereinafter "Hr'g Tr."]). SWN presented clear and convincing evidence that the Tax Department failed to consider SWN's actual operating expenses in determining the valuation for the wells assessed for Marshall County. SWN presented a complete analysis of its actual operating expenses from the state and local tax firm Altus Group US, Inc. ("Altus"), supported by testimony from an Altus Director, Kirsten Evans, that correctly applies the approach to arrive at allowable operating expenses. (*See* Hr'g Tr., pp. 12-57).

SWN also proved by clear and convincing evidence that the State erroneously calculated average operating expenses at the lesser of 20% of gross receipts or $175,000. Altus explained that by artificially capping operating expenses at $175,000, which is not permitted by the legislative rule, the State is grossly overvaluing the fair market value of SWN's wells. (Hr'g Tr., at pp. 13:22-14:5; 33:11-13; 34:3-5; 34:12-14; 50:2-7; 57:19-22). The State also does not take into account SWN's point-of-sale, and the operating expenses incurred to get the gas downstream to market. (Hr'g Tr. at p. 50:8-55:19; Hr. Tr. Exh. 16).

Despite the clear and convincing evidence produced by SWN, the Board made no adjustment to the Tax Department's valuation. (See Ex. B to SWN's Petition). SWN timely

petitioned the Court for appeal of the Board's decision. In its petition, SWN alleges that the Tax Department abused its discretion by failing to consider SWN's actual and allowable operating expenses in a manner contrary to the statutes, regulations and official releases from the Tax Department governing valuation of personal property, and that the Tax Department has failed to support its valuation with substantial evidence.

In its Complaint, SWN alleges that (1) the Tax Department failed to properly calculate the fair market value of its Marcellus wells, (2) the Tax Department improperly placed a "cap" on operating expenses, resulting in an inflated value of SWN's wells, (3) the Tax Department calculated an inaccurate "cap," (4) the Tax Department treats similarly situated tax payers differently in violation of United States Constitution and the West Virginia Constitution, as the "cap" of $175,000 only adversely affects tax payers that have wells with gross receipts over a certain threshold; and (5) the Tax Department's valuation of SWN's wells did not properly account for operating expenses for wells that produced both oil and gas receipts.

SWN's asks the Court to find that the Board incorrectly made no changes to the Tax Department's valuation; that the State's "cap" of $175,000 in operating expenses be removed; that SWN's operating expense percentage of 56.4% per well be applied to its Marshall County wells; that a combined amount of operating expenses for oil receipts and gas receipts, and not a weighted average, be applied; and that the value of SWN's Marshall County gas wells for the 2017 tax year be set at $70,909,245.

Because the issues in this matter are complex and require specialized knowledge regarding taxation of oil and gas wells, specialized treatment will improve the expectation of a fair and reasonable resolution of this matter. Accordingly, SWN requests that this matter be transferred to the Business Court Division.

II. APPLICABLE LEGAL STANDARD

West Virginia Trial Court Rule 29.06 provides that "[a]ny party . . . may seek a referral of Business Litigation to the [Business Court] Division by filing a Motion to Refer to the Business Court Division with the Clerk of the Supreme Court of Appeals of West Virginia." Tr. Ct. R. 29.06(a). "Business Litigation" is defined as follows:

> (a) "Business Litigation"-- one or more pending actions in circuit court in which:
>
> (1) the principal claim or claims involve matters of significance to the transactions, operations, or governance between business entities; and
>
> (2) the dispute presents commercial and/or technology issues in which specialized treatment is likely to improve the expectation of a fair and reasonable resolution of the controversy because of the need for specialized knowledge or expertise in the subject matter or familiarity with some specific law or legal principles that may be applicable; and
>
> (3) the principal claim or claims do not involve: consumer litigation, such as products liability, personal injury, wrongful death, consumer class actions, actions arising under the West Virginia Consumer Credit Act and consumer insurance coverage disputes; non-commercial insurance disputes relating to bad faith, or disputes in which an individual may be covered under a commercial policy, but is involved in the dispute in an individual capacity; employee suits; consumer environmental actions; consumer malpractice actions; consumer and residential real estate, such as landlord-tenant disputes; domestic relations; criminal cases; eminent domain or condemnation; and administrative disputes with government organizations and regulatory agencies, provided, however, that ***complex tax appeals are eligible to be referred to the Business Court Division***.

W. Va. Trial Ct. R., 29.04 (emphasis added).

III. ANALYSIS

This is a complex tax appeal that should be referred to the Business Court Division. The tax assessment issues in this case are technical, and are precisely the type of issues that should be referred to the Business Court Division. *See* Trial Ct. R., 29.04(a)(3) (providing that "complex tax appeals are eligible to be referred to the Business Court Division."). Further, this case

"involve[s] matters of significance to the transactions, operations, or governance between business entities," and "presents commercial and/or technology issues in which specialized treatment is likely to improve the expectation of a fair and reasonable resolution of the controversy." *See* Trial Ct. R., 29.04(a)(1)-(2).

Here, SWN is challenging the Tax Department's valuation of its Marcellus wells in Marshall County. Before the Board, SWN submitted proof of its actual operating expenses, which it contends should be used in determining the value of its Marcellus wells. (*See* Hr'g Tr., pp. Hr'g Tr., pp.12-57; Hr'g Tr. Exhibits 3, 4, 6, 7, 9(A)-(E), 14, 17A, 18). SWN also demonstrated that the State does not take into account SWN's point-of-sale for the gas, or the operating expenses incurred to get the gas downstream to market. (Hr'g Tr. at p. 50:8-55:19; Hr. Tr. Exh. 16). Analysis of these issues requires an understanding of SWN's business model, particularly with regard to the point-of-sale, and an understanding of allowed operating expenses under Section 3.16 of Series 1J, Title 110 State Tax Department Legislative Rule for Valuation of Producing and Reserve Oil & Natural Gas for Ad Valorem Property Tax Purposes.

SWN also demonstrated to the Board that the Tax Department calculated an inaccurate "cap" with respect to allowed operating expenses. SWN explained that by artificially capping operating expenses at $175,000, which is not permitted by the legislative rule, the State is grossly overvaluing the fair market value of SWN's wells. (Hr'g Tr., at pp. 13:22-14:5; 33:11-13; 34:3-5; 34:12-14; 50:2-7; 57:19-22).

Thus, this tax appeal presents "issues in which specialized treatment is likely to improve the expectation of a fair and reasonable resolution of the controversy." *See* Trial Ct. R., 29.04(a)(2). In order to fairly and reasonably resolve these issues, the decision-maker should have familiarity with the tax code, the mechanisms used to value taxable property, the mass

appraisal system used to assess oil and gas wells (including the methodology set forth in § 110-1J-4.1 is reflected in Tax Department's 2017 Administrative Notice), as well as familiarity with allowable operating expenses under Section 3.16 of Series 1J, Title 110. As demonstrated in the hearing transcript and exhibits (attached to SWN's complaint), SWN has placed clear and convincing evidence on the record as to why its Marcellus wells have been overvalued. SWN asserts that specialized knowledge on the above-mentioned issues would improve the likelihood that the submitted documentation and testimony is fairly considered, and that a reasonable resolution of this controversy will result.

Furthermore, several tax matters have been referred to the Business Court Division. *See e.g., Lee Trace LLC v. Berkeley County Council as Board of Review and Equalization, et al.*, Case Nos. 11-AA-2 and 14-AA-1, 2015 WL 7628718 (W. Va. Nov. 20, 2015) (deciding Lee Trace LLC's appeal of the Business Court Division's decision related to its challenge of its property tax assessments, including that it did not receive proper notice of its right to appeal its assessment, that the assessor did not consider the requisite depreciation factors, and that the assessor failed to consider income information); *Matkovich v. University Healthcare Foundation, Inc.*, 238 W.Va. 345, 795 S.E.2d 67 (2016) (deciding whether a parcel of real property is exempt from *ad valorem* property tax); *John Skidmore Trucking, Inc. v. Mark W. Matkovich*, Case No. 14-C-27, Braxton County Circuit Court, Business Court Division (involving an assessment for sales and use tax related to services provided by an Enrolled Agent); as well as matters pertaining to essentially the same issues raised by SWN, including *Consol Energy dba Gas Company LLC v. Dale* Steager, et al. Case No. 17-AA-2, Doddridge County Circuit Court, Business Court Division; *Consol Energy dba Gas Company LLC v. Dale* Steager, et al. Case No. 17-C-11, Lewis County Circuit Court, Business Court Division; *Consol Energy dba Gas*

Company LLC v. Dale Steager, et al. Case No. 16-C-135, McDowell County Circuit Court, Business Court Division; *Antero Resources Corporation v. Dale Steager, et al.*, Case No. 17-AA-1, Doddridge County Circuit Court, Business Court Division and *Antero Resources Corporation v. Dale Steager, et al.*, Case No. 17-AA-3, Doddridge County Circuit Court, Business Court Division and *Antero Resources Corporation v. Dale Steager, et al.*, Case No. 17-AA-1, Ritchie County Circuit Court, Business Court Division. The issues presented in this case similarly qualify for transfer under W.Va. Trial Court Rule 29.

Finally, because this case is in the early stages of litigation, referral to the business court would not prejudice the Respondents or waste judicial resources. Instead, it is in the interest of the parties and judicial economy for the above-referenced related cases to be consolidated and referred to the Business Court Division. Absent transfer and consolidation, two different circuit courts and two different judges will have to hear and decide the same issue, possibly reaching inconsistent results. Thus, not only is this case exactly the type that should be referred to the Business Court Division, but consolidation in the Business Court Division will also promote judicial economy and consistency. For all of these reasons, this case should be referred to the Business Court Division.

In further support of this Motion, please find attached hereto an accurate copy of the operative complaints, answers, and docket sheet.

IV. CONCLUSION

WHEREFORE, the undersigned hereby moves, pursuant to W.Va. Trial Court Rule 29, the Chief Justice of the West Virginia Supreme Court of Appeals to refer this case to the Business Court Division.

Respectfully submitted, this 5th day of April, 2018.

SWN PRODUCTION COMPANY, LLC

By Counsel

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John J. Meadows (WVSB No. 9442)
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Charleston, West Virginia 25326
Telephone (304) 353-8000
Facsimile (304) 353-8180

CERTIFICATE OF SERVICE

I, John Meadows, do hereby certify that on this 5th day of April, 2018, I have served the foregoing ***"Motion to Refer Case to Business Court Division,"*** with attachments by first class mail to all counsel of record at the addresses provided below:

L. Wayne Williams, Esquire
Assistant Attorney General
1900 Kanawha Boulevard, East
Building 1, Room W-435
Charleston, WV 25305

County Commission of Marshall County
P.O. Drawer B
700 6th Street
Moundsville, WV 26041

The Marshall County Assessor
700 6th Street
PO Box 554
Moundsville, WV 26041

John J. Meadows (WVSB No. 9442)

West Virginia Circuit Express (/DEFAULT.ASPX)

Civil

Case Information

Second Judicial Circuit of Marshall County

18-C-8

Judge: JEFFREY D. CRAMER

SWN PRODUCTION COMPANY, LLC VS. THE HONORABLE DALE STEAGER

Plaintiff(s)	Plaintiff Attorney(s)
LLC, SWN PRODUCTION	STEPTOE & JOHNSON

Defendant(s)	Defendant Attorney(s)
STEAGER, DALE	
COUNTY COMMISSION OF MARSHALL	
KESSLER, CHRISTOPHE	N/A

Date Filed: 01/16/2018
Case Type: MISCELLANEOUS CIVIL
Appealed: 0
Final Order Date: N/A
Statistical Close Date: N/A

Line	Date	Action / Result
0001	01/16/2018	COMPLAINT, CCIS & SUMMONS FILED; ISSUED TO SHERIFF FOR SERVICE
0002		ON KESSLER & COUNTY COMMISSION; SUMMONS SIGNED & GIVEN TO ATTNY
0003		FOR SERVICE ON HONORABLE DALE STEAGER (EXHIBIT 18 FILED UNDER
0004		SEAL) **EXHIBITS COULD NOT BE SCANNED AS THEY WERE PRINTED ON
0005		BOTH SIDES OF PAPER**
0006	01/17/2018	RET. SUMMONS SERVED THE COUNTY COMMISSION OF MARSHALL CO. SIGNED
0007		BY BETSY FROHNAPFEL ON 01/17/18.
0008	01/17/2018	RET. SUMMONS SERVED THE HON. CHRISTOPHER J. KESSLER SIGNED BY
0009		BETTY CARNEY ON 01/17/18.
0010	01/31/2018	MOTION TO DISMISS ON BEHALF OF THE HONORABLE CHRISTOPHER J.
0011		KESSLER; CERT.OF SERVICE. (TMU)
0012	01/31/2018	MOTION TO DISMISS THE COUNTY COMMISSION OF MARSHALL CO. SITTING
0013		AS A BOARD OF ASSESSMENT APPEALS;CERT.OF SERV.; ORDER FOR SIGN.

Circuit Express Printable Report

0014		FILE SENT TO JUDGE CRAMER. (TMU)
0015	01/31/2018	NOTICE OF APPEARANCE, CERT OF SERVICE./MHM
0016	02/02/2018	RETURN OF SERVICE./MHM
0017	02/06/2018	FAX: ANSWER OF THE WV.STATE TAX DEPT. TO COMPLAINT OF PETITIONER
0018		SWN PRODUCTION CO.,LLC; CERT.OF SERV.; CCIS. (TMU)
0019	02/08/2018	RECEIVED ORIGINALS FOR DOCKET LINE 17 & 18. (TMU)