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## **Testimony to Kansas House Tax Committee**

### **House Bill 2701**

**An Act concerning property taxation; relating to oil and gas leases or properties;  
determination of value of production, evidence**

**Edward P. Cross, President  
Kansas Independent Oil & Gas Association**

**March 3, 2016**

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Good afternoon Chairman Kleeb, Vice Chairman Suellentrop, Ranking Minority Member Sawyer and members of the committee. I am Edward Cross, President of the Kansas Independent Oil & Gas Association (KIOGA). KIOGA represents thousands of independent oil and natural gas explorers and producers, as well as allied service and supply companies. Our members account for 86% of the oil and 63% of the natural gas produced in Kansas. With over 4,200 members across the entire state, KIOGA is the lead state and national advocate for the Kansas independent oil and natural gas industry. I am responsible for public policy advocacy and interaction with external stakeholders including elected officials, regulators, governmental decision-makers, and community leaders. I am here this afternoon to oppose HB 2701 as written and to offer an amendment for consideration.

Over 99% of the properties in the state do not have valuation disputes that cannot be settled between the producer and the County Appraiser through an informal hearing. For those that go to the Board of Tax Appeals (BOTA), the issues are most often matters of decline rate affecting the present worth factor or the consideration of excess expenses which must be normal and recurring in order to be considered. In those instances, the additional information which would be available due to the passage of time would tend to allow BOTA to issue a more informed opinion. Over the years, the courts have allowed information after the valuation date because it would tend to validate the claims of one party or another. Neither the producer nor

the County intrinsically gains an advantage by the use of additional evidence. The advantage is only gained if the evidence would support their position. This evidence would be available to either party. The result of the change proposed by HB 2701 would be to preclude the use of that evidence, which would limit BOTA's ability to arrive at the fairest valuation possible.

I understand that the problem Counties were hoping to correct was the repayment of taxes several years after the assessment period. Some oil and gas producers pay their second half taxes under protest and take these cases to BOTA. Nothing in HB 2701 would change the availability of that practice. It would only limit the evidence that could be presented to BOTA.

If the Counties are repaying large amounts of tax several years after the assessment, it may be because the initial assessments were far too large. Perhaps the taxpayer is the aggrieved party in those instances. It seems that the problem encountered by the Counties would need to be addressed by limiting the appeals process, not just for oil and gas but for all taxpayers.

As I said, KIOGA opposes HB 2701 as written because it would limit the evidence which could be considered in valuing an oil and gas property to information regarding production for the first three months following the appraisal date. HB 2701 would overrule a Kansas Supreme Court case *Board of Ness County Commissioners vs. Bankoff Oil Co.*, 265 Kan. 525, 960 P.2d 1279 (1998). HB 2701 would not allow the appraiser or the courts to consider much of the evidence which is currently now considered in the most contentious of valuation disputes. Exclusion of evidence is generally contrary to the principles of equity and should only be used in limited circumstances. Also, HB 2701 (as written) attempts to change substantive rights through a retroactive application of the law. It is well-settled in Kansas, if a statute's retroactive application will affect vested or substantive rights, its retroactive application cannot be enforced. A taxpayer's right to a refund of its ad valorem taxes is a vested and substantive right.

Perhaps a compromise could be considered. In the *Bankoff* case, the Kansas Supreme Court allowed consideration of production data through June 30<sup>th</sup>. We offer an amendment to HB 2701 to allow information used to establish the fair market value of producing oil and gas leases be limited to any information regarding production prior to July 1 of the calendar year in which such property is assessed. In addition and in accordance with the court case *Owen Lumber Co. v. Chartrand*, 276 Kan. 218, 220, 73 P.3d 753, 755 (2003), we suggest avoiding making HB 2701 retroactive by striking the language in HB 2701 Section 1 (e) and replacing with "*The provisions of this act shall apply to all tax years commencing on and after December 31, 2016.*"

I appreciate the opportunity to provide these comments. Thank you for your time and consideration. I stand for questions.

**HOUSE BILL No. 2701**

By Committee on Taxation  
2-12

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AN ACT concerning property taxation; relating to oil and gas leases or properties; determination of value of production, evidence; amending K.S.A. 2015 Supp. 79-331 and repealing the existing section.

*Be it enacted by the Legislature of the State of Kansas:*

Section 1. K.S.A. 2015 Supp. 79-331 is hereby amended to read as follows: 79-331. (a) Except as otherwise provided in subsection (b) of this section, in determining the value of oil and gas leases or properties the appraiser shall take into consideration the age of the wells, the quality of oil or gas being produced therefrom, the nearness of the wells to market, the cost of operation, the character, extent and permanency of the market, the probable life of the wells, the quantity of oil or gas produced from the lease or property, the number of wells being operated, and such other facts as may be known by the appraiser to affect the value of the lease or property.

Whenever a change in any of the factors or figures used in determining the 8/8ths valuation of the production for any oil or gas lease or property is made pursuant to the tax equalization, tax protest or tax grievance proceedings, such change shall apply to the working interest, royalty interest, overriding royalty interest and production payments and, if applicable, a refund of taxes shall be made in the manner prescribed by ~~subsection (1)(1) of K.S.A. 79-2005(1)(1)~~, and amendments thereto.

(b) The valuation of the working interest and royalty interest, except valuation of equipment, of any original base lease or property producing oil or gas for the first time in economic quantities on and after July 1 of the calendar year preceding the year in which such property is first assessed shall be determined for the year in which such property is first assessed by determining the quantity of oil or gas such property would have produced during the entire year preceding the year in which such property is first assessed upon the basis of the actual production in such year and by multiplying the income and expenses that would have been attributable to such property at such production level, excluding equipment valuation thereof, if it had actually produced said entire year preceding the year in which such property is first assessed by 60%.

(c) The provisions of subsection (b) of this section shall not apply in the case of any production from any direct offset well or any subsequent

well on the same lease.

(d) (1) In order to clarify and express the intent of the legislature regarding the methodology utilized in the determination of fair market value of producing oil and gas leases for property tax purposes, it is hereby declared that the primary and predominant consideration in such determination is, has been and shall be the actual value of oil and gas production severed from the earth.

(2) *Information used to establish the fair market value of producing oil and gas leases shall be limited to any information regarding production prior to ~~April 1~~ **July 1** of the calendar year in which such property is assessed.*

(e) The provisions of this act shall apply to all tax years commencing on and after December 31, ~~2003~~ **2016**.

Sec. 2. K.S.A. 2015 Supp. 79-331 is hereby repealed.

Sec. 3. This act shall take effect and be in force from and after its publication in the statute book.