

**JURISDICTION:** OKLAHOMA TAX COMMISSION - DECISION  
**CITE:** 2000-08-03-012 / NOT PRECEDENTIAL  
**ID:** P9500003  
**DATE:** 08-03-00  
**DISPOSITION:** DENIED  
**TAX TYPE:** SALES  
**APPEAL:** OK SUP CT. 90,043 / REVERSED AND REMANDED;  
NO APPEAL ON REMANDED ORDER

### FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above styled and numbered cause was originally tried on July 30, 1996. Findings, Conclusions and Recommendations WERE ISSUED in THIS cause on June 30, 1997, which were adopted as the Order of the Oklahoma Tax Commission. Oklahoma Tax Commission Order No. 97-08-12-034. Protestants appealed said Order to the Oklahoma Supreme Court. The Court of Civil Appeals of the State of Oklahoma, Division III, reversed the Order of the Tax Commission by unpublished decision and remanded the same for further proceedings to determine the value of the tangible personal property included in the 1991 sale of a gas gathering system.

Upon review of the file and records, including the record of the hearing, the exhibits received into evidence, the testimony of MR. ACCOUNTANT, PROTESTANT OFFICER and MR. ANONYMOUS from the prior proceedings, the briefs and arguments of the parties and the proposed Findings, Conclusions and Recommendations submitted by the parties, the ADMINISTRATIVE LAW JUDGE HEREIN MADE CERTAIN FINDINGS WHICH, AS CORRECTED AND AMENDED BY THE COMMISSION, WERE ADOPTED AS ITS ORDER HEREIN.

### FINDINGS OF FACT

1. In April, 1991, THE CORPORATION sold a gas gathering system known as SYSTEM 1, located in COUNTY 1, Oklahoma, and the marketing rights to the gas gathering systems known as SYSTEM 2, located in COUNTY 2, Oklahoma and ANONYMOUS County, OUT OF STATE, respectively, to COMPANY 1 for One Million Dollars (\$1,000,000.00).

2. The sale of SYSTEM 1 included intangible assets (including, but not limited to certain gas purchase contracts, right-of-ways, easements, gathering and transportation agreements, equipment leases and service contracts and licenses and permits) and tangible assets (including fence, fittings and connectors for compressors, two and three-eighths inch line pipe, six and five-eighths inch line pipe, two and seven-eighths inch line pipe, six inch line pipe, three inch line pipe, six inch poly pipe, valves, meter runs and fittings, miscellaneous fittings and connections, a natural gas odorizer, a 550 gallon oil

tank, a 100 barrel fiberglass water tank, a propane tank, a gas volume tank, and an American Recorder).

3. PROTESTANT OFFICER testified at the first hearing that he purchased an incomplete SYSTEM 1 in place in 1989 for "somewhat less than two hundred thousand". The purchase price included equipment, right-of-ways and gas purchase contracts. He stated that the "[seller] hadn't laid much physical assets". PROTESTANT OFFICER also testified that "we put about another two hundred thousand in [the system] with acquisition of additional right-of- way, labor, this polyethylene pipe".

4. According to PROTESTANT OFFICER, tangible personal property sold with SYSTEM 1 "represented no more than twenty-five percent of the value of the purchase price, if that". He stated that the difference between the value he attached to the tangible personal property and the value of twenty-five thousand attached to the property by MR. ANONYMOUS was that MR. ANONYMOUS was valuing the system in a dormant stage whereas, he valued it as an ongoing concern as it was when COMPANY 1 acquired the system. He further stated that the value of the hard assets which were in place in the system as it operated in the ground and above the ground "would probably have been somewhere between two and four hundred thousand dollars".

5. PROTESTANT OFFICER admitted that Section II E of the Sales Agreement, Allocation of Purchase Price, reported an allocation of Nine Hundred and Seventy Five Thousand Dollars to "pipeline and other equipment" and no allocation of purchase price to SYSTEM 2 or to the contract rights or incidental rights. He testified that although none of the purchase price was allocated to contract or incidental rights, the acquisition of such right was the reason why the system sold for what it did.

6. PROTESTANT OFFICER also admitted that Form 8594, Asset Acquisition Statement Under Section 1060 of the Internal Revenue Code, filed with THE CORPORATION'S 1991 Federal Income Tax Return reported an allocation of the purchase price to the pipeline which closely approximated the amounts on Schedule II E of the Sales Agreement. Schedule II E of the Sales Agreement contains a provision whereby the parties agreed to file Form 8594 consistent with the allocation of purchase price under Schedule II E.

7. Form 8594 was filed for compliance reasons with the Internal Revenue Code. The form does not set the value agreed to by the parties for the tangible personal property conveyed under the Sales Agreement. Further, the allocation of the purchase price as reported on Form 8594, as filed, was incorrect as it included not only intangibles, but tangible assets.

8. PROTESTANT OFFICER identified the General Ledger of THE CORPORATION for the period ended March 31, 1991. The ending balance for "Total Pipeline System" is

reported as \$415,796.32. Less accumulated depreciation the ending balance for "Total Fixed Assets" is reported as \$227,126.25. PROTESTANT OFFICER testified that the amounts reported on the general ledger not only included SYSTEM 1, but also systems in COUNTY 3 and COUNTY 4 and some equipment in AN ANONYMOUS AREA OF Oklahoma.

9. PROTESTANT OFFICER also testified that the amounts reported for "Buildings and other depreciable assets" on the balance sheet filed with the 1991 Federal Income Tax Return (Beginning of tax year-\$765,424, End of tax year-zero) were incorrect since they did not sell all of their depreciable assets in 1991.

10. MR. ANONYMOUS testified at the first hearing that he estimated the fair market value of the tangible personal property associated with SYSTEM 1 to be \$25,000.00. He stated that his estimate was based on what they could expect to receive in a depressed gas market for the tangible personal property if the property was sold by itself without the contract rights or right-of-ways. He further stated that his estimate was based on 1991 values although he prepared the estimate in 1993.

11. MR. ACCOUNTANT, A Certified Public Accountant, testified at the first hearing and the second hearing in this cause. At the first hearing, MR. ACCOUNTANT testified that Form 8594, as filed with the 1991 Federal Income Tax Return was incorrect in that it included tangible assets in Class III property. He stated that Form 8594 is merely an informational form and that an amended Form 8594 was filed for 1991, however, it was also incorrect. He further stated that Class III property should have included only pipeline contracts and right-of-ways and that the amount reported should have been approximately \$740,000.00.

12. At the second hearing, MR. ACCOUNTANT testified concerning an analysis he prepared shortly after the first hearing regarding the tangible personal property sold to COMPANY 1 in 1991. He stated that THE CORPORATION purchased the tangible personal property related to SYSTEM 1 in 1989 for \$233,790.00. The purchase price of the tangible personal property was determined from THE CORPORATION'S books and records, and depreciation schedule. He further testified that the book value of the tangible personal property was \$133,595.00 as of the date of the sale. The book value of the tangible personal property was determined by subtracting accumulated depreciation from the total historical cost of the tangible personal property. MR. ACCOUNTANT admitted that the accumulated depreciation number was an estimate and that depreciation is not a relevant number in determining fair market value. MR. ACCOUNTANT'S analysis of the value of the tangible personal property also does not include the additional assets added to the system as testified to by PROTESTANT OFFICER since the write up on his analysis indicates "[w]e are talking about a fence, some oil tanks, and some pipe that initially cost in 1989 only \$233,790 . . ."

13. MR. AUDITOR, with the Ad Valorem Division of the Tax Commission, testified that he is responsible for the valuation of public service corporations and that THE CORPORATION was a public service corporation in 1991. MR. AUDITOR identified a Notice of Valuation issued to THE CORPORATION on June 10, 1991. The Notice reports a fair cash value of THE CORPORATION'S property in Oklahoma as of January 1, 1991, of \$452,000.00. MR. AUDITOR testified that the assessed value was an estimate based on the best evidence the Tax Commission had at the time. He stated that THE CORPORATION'S 1991 Franchise Tax Return was primarily used in determining the property owned by THE CORPORATION. He stated that the balance sheet to the Franchise Tax Return does not indicate whether contract rights or right of ways were included in fixed depreciable assets. MR. AUDITOR further testified that THE CORPORATION did not dispute the valuation, however, he also testified that the Notice of Insufficient Information and Notice of Valuation were issued to THE CORPORATION on the same day and that THE CORPORATION was not notified that it could contest the valuation. MR. AUDITOR also stated that no one from the Tax Commission actually viewed THE CORPORATION'S property.

### **ISSUES AND CONTENTIONS**

The issue presented for decision is whether Protestants sustained their burden of proving that the amount of the purchase price allocated to the tangible personal property by the Division is incorrect. If the first issue is answered in the affirmative, then the issue becomes what amount of the purchase price is allocable to the tangible personal property or what is the fair market value of the tangible personal property.

Protestants contends that the fair market value of the tangible personal property as of the date of the sale was \$25,000.00. In support of this contention, Protestants cite the testimony of MR. ANONYMOUS. In the alternative, Protestants contend that the amount of the purchase price allocable to the tangible personal property should be based on the book value of the property or \$133,595.00. In support of this contention, Protestants cite the testimony of MR. ACCOUNTANT.

The Division contends that the protest should be denied since Protestants failed to present evidence sufficient to prove an adjustment to the value assigned to the tangible personal property by the Division. In support of this contention, the Division argues that the testimony of Protestants' witnesses was conflicting as to the value of the tangible personal property and that said testimony without substantiation through documentation is insufficient to establish a value different than the one contemporaneously determined by the Ad Valorem Division.

**CONCLUSIONS OF LAW**

1. Jurisdiction over the parties and subject matter of this proceeding is vested in the Tax Commission. 68 O.S. 1991, § 207.

2. Sales tax is levied on the gross receipts or gross proceeds of each sale of tangible personal property. 68 O.S. 1991, § 1354(1)(A).

3. "Tangible personal property" is defined to mean "personal property which may be seen, weighed, measured, felt, or touched or which is in any other manner perceptible to the senses." 68 O.S. 1991, § 1352(N). The phrase "tangible personal property" is all inclusive, and is not limited except by specific exemption. ***Magnolia Petroleum Co. v. Oklahoma Tax Commission***, 326 P.2d 821 (Okla. 1958).

4. The terms "gross receipts" or "gross proceeds" are defined in part to mean "the total amount of consideration for the sale of any tangible personal property . . . whether the consideration is in money or otherwise." 68 O.S. 1991, § 1352(F). Where a transaction involves real property and/or intangible personal property, as well as tangible personal property, the gross receipts or gross proceeds paid for the property must be allocated among the various types of property for purposes of determining the amount of sales tax payable as a result of such transaction. ***Magnolia***, supra. See, ***WEBR, Inc. v. State Tax Commission***, 397 N.Y.S.2d 200, 58 A.D.2d 471 (App.Div. 1997)<sup>1</sup>.

5. A proposed assessment is presumed correct and the taxpayer bears the burden of showing that it is incorrect, and in what respect. ***Enterprise Management Consultants, Inc. v. Oklahoma Tax Commission***, 768 P.2d 359 (Okla. 1988). Failure to provide evidence which is sufficient to show an adjustment to the proposed assessment is warranted will result in the denial of the protest. ***Continental Oil Company v. Oklahoma Tax Commission***, 570 P.2d 315 (Okla. 1977). The burden of proving a sale is not a taxable sale is on the person who made the sale. 68 O.S. 1991, § 1365(C).

6. "Fair market value" is that value or price which a willing purchaser would pay and a willing seller would accept under ordinary circumstances. ***Onego Corporation v. United States***, 295 F.2d 461, 463 (10th Cir. 1961). See, ***FinaServe, Inc. v. Oklahoma Tax Commission***, 828 P.2d 440 (Okla.App. 1991). In ***FinaServe***, the Court held that the Commission's assessment of sales tax on the net book value of equipment transferred as a part of the sale of gasoline stations was erroneous. The Court reasoned:

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<sup>1</sup>In this case the Appellate Division of the Supreme Court of New York considered a transaction involving the sale of both tangible personal property and real property and held that "the Tax Commission had the right, indeed, the obligation, to arrive at a fair sales price of the personal property for sales tax purposes."

By itself, the net book value of equipment does not accurately gauge the equipment's worth to the buyer of the realty upon which the seller's equipment was used. Book value is only a statement of market value, determined years before, less depreciation. Book value of equipment reveals nothing about the *present* sale value placed on the equipment by a buyer and seller. A fact finder may not properly ignore the facts of a rising or falling market, or of obsolescence of the equipment. *Id.*, at 442-443. (Emphasis original).

7. The best evidence as to the fair market value of the tangible personal property at issue in this cause comes from the testimony of PROTESTANT OFFICER. PROTESTANT OFFICER refuted the value placed on the property by MR. ANONYMOUS, stating that MR. ANONYMOUS valued the property in a dormant stage, not as a going concern, but on a piece by piece basis and in reference to a depressed gas market. PROTESTANT OFFICER'S valuation not only took into account the historical cost of the property, but also that it was sold as a going concern at a time of high expectations as to the gas production in the field. MR. ACCOUNTANT'S valuation is at best suspect since he admitted that the accumulated depreciation was only an estimate and the valuation did not take into account the additional property added to SYSTEM 1 after 1989.

8. Based on the evidence presented, the undersigned finds that the fair market value of the tangible personal property included in the 1991 sale of SYSTEM 1 to COMPANY 1 was \$250,000.00. The undersigned further finds that the sales tax deficiency due and owing by Protestants should be calculated and fixed upon the \$250,000.00.

### DISPOSITION

Based on the above and foregoing findings of fact and conclusions of law, it WAS DETERMINED that the fair market value of the tangible personal property included in the 1991 sale of SYSTEM 1 be determined to be \$250,000.00. It WAS further DETERMINED that the sales tax deficiency due and owing by Protestants should be calculated and fixed upon the \$250,000.00.

### OKLAHOMA TAX COMMISSION

**CAVEAT:** This decision was **NOT** deemed precedential by the Commission. This means that the legal conclusions are not generally applicable or are limited in time and/or effect. Non-precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.