



Mike Kadas
Director

Montana Department of Revenue



Steve Bullock
Governor

MEMORANDUM

TO: Revenue and Transportation Interim Committee

FROM: Dan Whyte, Chief Legal Counsel

DATE: September 8, 2016

SUBJECT: Department of Revenue Major Case Update

MONTANA SUPREME COURT

Alpine Aviation: Alpine Aviation has been centrally assessed by the Department since it began operating in Montana in the late 1990s. Alpine filed an appeal with the Office of Dispute Resolution, and then with the Montana Tax Appeal Board (MTAB), arguing that it does not meet the definition of a centrally assessed company because it is not a “regularly scheduled airline” as defined in federal law. The Department asked the District Court to determine the meaning of “scheduled airline” and “scheduled air commerce” for Montana property tax purposes. On May 14, 2015, the First Judicial District Court ruled that “regularly scheduled flights” are those flights which follow a pattern, but are not necessarily uniform intervals according to timetables and locations predefined by the carrier, and which fly regardless of whether there are passengers or freight carried. The matter was appealed to the Montana Supreme Court. The parties have completed briefing and are awaiting a decision from the Court.

Richland Aviation: Richland filed a declaratory judgment action in the 7th Judicial District Court, Richland County, challenging the Department’s classification of Richland’s property for tax year 2015 as subject to central assessment. Richland filed a motion for summary judgment arguing that it is not a “scheduled airline” as that term is used and understood in Montana law. Richland’s summary judgment motion was fully briefed and argued. On August 1, 2016, the District Court entered an Order granting Richland’s Motion for Summary Judgment and ruling that a “‘scheduled’ airline must hold itself out to the public (typically by publishing flight schedules) that it operates between designated points regularly.” The Department appealed to the Montana Supreme Court. The Department’s Opening Brief is to be filed by September 26, 2016.

FEDERAL DISTRICT COURT

LL, Liquor, Inc., v. State of Montana, et al.: During the 2015 Legislative Session, the Legislature passed Senate Bill No. 193, which changed the complicated three-piece commission rates received by the agency liquor stores to a single percentage rate based on sales. The commission rate percentages range from 12.15% commission for stores that purchase more than \$7,000,000 worth of liquor, to 16% commission for stores that purchase no more than \$250,000 worth of product. It has been reported that this amendment to the commission rates will result in a revenue increase for 90 of the 96 agency liquor stores. One of the remaining six stores, LL Liquor, located in Lolo, Montana, has sued the State arguing that the State breached the contract with LL Liquor, and deprives LL Liquor of its property and contractual rights without due process of law, a constitutional violation. LL Liquor sought a preliminary injunction to stop implementation of the law, which was denied by the District Court. LL Liquor has appealed this issue to the 9th Circuit Court of Appeals. The parties await a decision from the oral argument before the 9th Circuit Court on April 6, 2016.

STATE DISTRICT COURT

CHS: The 2014 and 2015 disputes center on the market value of the Laurel Refinery. For the 2014 tax year, the company requested a market value of \$200 million, and the Department valued the refinery at \$848 million. Yellowstone CTAB determined a market value of \$510 million, and CHS and the Department each appealed that decision to the Montana Tax Appeal Board. Shortly after the parties initiated appeals before the Board and had agreed upon a January 2017 trial date, CHS filed a petition for interlocutory adjudication with the 13th Judicial District Court. The District Court dismissed CHS's petition on May 6, 2016, and CHS has 60 days to appeal that dismissal to the Montana Supreme Court. Respecting the 2015 tax year, the Yellowstone CTAB recently affirmed the Department's value (\$820 million), and CHS appealed that decision to the Montana Tax Appeal Board on May 12, 2016.

Hiland Crude, LLC: Hiland filed a declaratory judgment action in the 1st Judicial District Court challenging the Department's classification of Hiland's property for tax year 2014 as a pipeline carrier and, therefore, subject to central assessment. Trial is set for February 21, 2017. The matter is currently in discovery.

Kohoutek, et al.: Agency liquor store owners sought class certification and challenged the constitutionality of certain statutes. Specifically, agency liquor store owners alleged that § 16-2-101(2)(b)(ii)(B), MCA, is unconstitutional because it fails to fully compensate some liquor store owners for the mandatory 8% discount for unbroken case lot sales to licensees required by § 16-2-201, MCA. Plaintiffs filed in the 8th Judicial District Court, Cascade County. The Court bifurcated the issues (constitutionality and damages). On May 28, 2015, the Court determined that the statute violated the Plaintiffs' rights to substantive due process

and to equal protection of the law because the State has continued to use 1994 sales information to reimburse agency liquor stores for the mandatory case lot discounts.

On February 4 and 5, 2016, a bench trial was held addressing the damages phase. The District Court awarded \$14,722,297 in damages after concluding that the weighted average discount ratio statute became unconstitutional on July 1, 1998. A hearing on attorneys' fees and interest is set for December 2, 2016.

Lake County: On July 17, 1985, the Federal Energy Regulatory Commission (FERC) issued an *Order Approving Settlement and Issuing License* regarding the Kerr Project. The Order approved a settlement between the Confederated Salish Kootenai Tribes (CSKT) and the Montana Power Company (MPC) that included resolution of disputes over payments MPC made to CSKT for the use and occupancy of its lands and competing FERC license applications made by MPC and the CSKT. Under the Settlement, a 50-year license would jointly issue to MPC and the CSKT. The License provided that MPC would operate the project for 30 years, and then the CSKT could purchase the Project between the 30th and 40th years of the License under certain conditions outlined in the Settlement. Successors to MPC for the Kerr Project were PPL and NWE. The CSKT purchased the Kerr Dam from NWE on September 5, 2015. The FERC approved changing the name of the Kerr Project to Séliš Ksanka Qíispé (SKQ). The taxable value the Department apportioned to NWE for Kerr Dam for tax year 2015 was \$3.5 million.

The SKQ Property is located within the exterior boundaries of the Flathead Indian Reservation. The Department determined that because the property is tribal trust land and tribal improvements on tribal trust land owned by the CSKT, the property is no longer subject to taxation. Lake County filed a Writ of Mandamus on August 29, 2016, in the 20th Judicial District Court, challenging the Department's determination that (SKQ) Property is exempt from taxation under federal Indian law. Lake County claims the SKQ Property is taxable under state law and the NWE/Confederated Salish & Kootenai Tribes (CSKT) Deed. Lake County also claims it was not allowed to participate in the Department's decision-making process regarding the taxability of the SKQ Property.

The Department's Answer to Lake County's Writ of Mandamus is to be filed by October 14, 2016.

Omimex Canada, Ltd.: At issue is the Department's decision to classify Omimex's Montana property as a pipeline carrier and, therefore, subject to central assessment. The parties have agreed to consolidate the declaratory judgment actions for tax years 2011 and 2012, filed in the 2nd Judicial District, Silver Bow County, with the declaratory judgment actions for tax years 2013, 2014, and 2015 filed in the First Judicial District, and to transfer venue for all years to the First Judicial District Court, Lewis and Clark County. Judge Reynolds has assumed jurisdiction over all five pending tax years. Trial is scheduled for May 2017. Omimex filed for partial summary judgment on November 5, 2015, in the consolidated 2011-2015 matters. Omimex asks the Court to determine the meaning of "pipeline carrier" and whether

Omimex meets that definition, making the company subject to central assessment. The issues have been briefed and oral argument was held on May 25, 2016, and the parties await a decision.

Solem: The Solems filed a motion for class certification in the 11th Judicial District Court, Flathead County, challenging their land value, primarily arguing that the water influence used by the Department leads to improperly inflated values. The District Court recently granted class certification. The class certified is “all lakefront property owners in Neighborhood 800 who have timely paid under protest any portion of their property taxes since the last assessment cycle beginning in 2009.” Neighborhood 800 is the Somers/Lakeside area in which the Solem’s property is located. Between 2009 and 2015, approximately 200 taxpayers in Neighborhood 800 paid property taxes under protest.

A settlement conference is set for October 26, 2016.

MONTANA TAX APPEAL BOARD

Blixseth: The Department is pursuing Tim Blixseth’s tax debt. On March 20, 2015, the Department received final judgment against Mr. Blixseth before the Montana Tax Appeal Board on Mr. Blixseth’s appeal of the Department’s audit and assessment. Mr. Blixseth did not appeal any of the orders issued by the Montana Tax Appeal Board. Consequently, the Department has billed Mr. Blixseth in the approximate amount of \$74.4 million, and will begin pursuing Mr. Blixseth for collection. Dismissal of the involuntary bankruptcy petition remains on appeal before the United States District Court for the District of Nevada, where the matter is fully briefed. The Department has advised the United States District Court of the MTAB rulings, and the Department awaits a decision.

Plains Pipeline: Plains Pipeline has appealed the Department’s centrally assessed valuation of their property located in Montana to the Montana Tax Appeal Board. Plains Pipeline has also made allegations challenging classification. A weeklong trial before the Board is set for July 24, 2017. The parties are currently engaged in discovery.

Rocky Mountain Pipeline: Rocky Mountain Pipeline has appealed the Department’s centrally assessed valuation of their property located in Montana to the Montana Tax Appeal Board. A weeklong trial before the Board is set for April 24, 2017. The parties are currently engaged in discovery.

DOR OFFICE OF DISPUTE RESOLUTION

NaturEner: NaturEner has filed with the Office of Dispute Resolution three separate appeals of the Department’s 2015 assessments. At issue is the Department’s valuation of NaturEner’s three windfarms: Glacier Wind Energy 1, LLC, Glacier Wind Energy 2, LLC, and Rim Rock Wind Energy, LLC. The matter awaits a schedule for discovery and trial. The parties attempted mediation on July 12, 2016, but were unsuccessful. The parties anticipate

engaging in mediation again in early fall based on the availability of new information. NaturEner has also appealed for the 2016 tax year.

VisionNet: In July, VisionNet appealed the Department's 2015 assessment to the Office of Dispute Resolution. Generally, VisionNet alleges the Department's classification of VisionNet is improper. VisionNet also contests its market value assessment as improperly including intangible personal property and use of improper capitalization rates. An initial conference was held with ODR on September 30, 2015. VisionNet has filed a declaratory judgment action before the First Judicial District Court. The Department filed an answer to the complaint on May 18, 2016. A four-day bench trial is set for October 10, 2017.

AT&T: AT&T appealed its 2016 valuation. AT&T mainly takes issue with the Department's deduction for intangible personal property and its weighting under the cost approach. An initial scheduling conference was held August 24, 2016, and both parties expressed interest in mediation. To date, no mediation has been selected or date for mediation has been set.

Phillips 66 Pipeline, LLC (Phillips): Phillips appealed its 2016 valuation to the ODR. Phillips mainly takes issue with the Department's cap rate and deduction for intangible personal property. The parties have yet to have their initial scheduling conference.

SETTLEMENTS

Priceline, et al. (Online Travel Companies): The Montana Supreme Court ruled that based upon the plain language of the Lodging Facility Use Tax, the online travel companies are not "owners" or "operators," as defined in statute, and, therefore, are not required to collect and remit the lodging tax on their fees. The lodging tax is 4%. However, the Court ruled that the online travel companies were, and are, required to collect and remit the 3% Sales Tax on their fees when selling, renting, or leasing accommodations and campgrounds. The Court further ruled that the online travel companies were also required to collect and remit a 4% Sales Tax on their fees related to the rental of vehicles. In ruling on damages owed by the companies, the Court rejected the online travel companies' argument that damages should be prospective, but limited the online travel companies' liability for the taxes from the filing of the Complaint, November 8, 2010. On August 28, 2015, the Supreme Court remanded the case back to Judge Seeley in the First Judicial District Court for consideration of the damages claims. Following the Supreme Court decision, the parties settled the tax revenues due to the state by the OTCs, at a total amount of \$1,367,167.07, and agreed on issues related to future compliance.