BEFORE THE STATE ASSESSMENT REVIEW BOARD
STATE OF ALASKA

In the Matter of:	)	
	)	Appeal of Revenue Decision
FURIE OPERATING ALASKA, LLC	)	No. 22-56-01
	)	
	)	
Oil & Gas Property Tax (AS 43.56)	)	OAH No. 22-0326-TAX
2022 Assessment Year	)	

CERTIFICATE OF DETERMINATION

The State Assessment Review Board convened on May 17, 2022 to hear an appeal by Furie Operating Alaska, LLC of Department of Revenue ("DOR") Informal Conference Decision 22-56-01. This ICD addresses the tax year 2022 assessment of Furie's oil and gas property related to the Kitchen Lights Unit ("KLU").

I. BACKGROUND

KLU is a Cook Inlet unit located in the Kenai Peninsula Borough. The assessed property is owned by:

Furie Operating Alaska, LLC
443 W. 9th Ave
Anchorage, AK 99501-3519

Furie's taxable KLU property includes an offshore platform, wells, production facilities, and a pipeline that transports gas from the platform to the onshore facilities.[1] KLU has been producing gas since November 2015, primarily from the Beluga formation. Furie has also produced from the Sterling formation, but encountered challenges with sand and high water content. Although Furie has not produced from the Sterling since 2019, its witnesses explained that Furie plans to test Sterling production in 2022.

In 2020, HEX Cook Inlet LLC acquired Furie in a bankruptcy auction for $34.2 million.

Each year, DOR assesses the value of oil and gas properties as of January 1 of that tax year. For production property, DOR determines value on a replacement cost less depreciation

[1] The Board uses the term "pipeline" in the general sense. Furie correctly pointed out that this pipeline is regulated as a field gathering line. *See* 11 AAC 80.055. Furie argued that because it is a gathering line, DOR should tax it as production property, not pipeline property. Furie admitted at the hearing, however, that the valuation would be the same.

basis.[2] Depreciation is based on the estimated life of proven reserves.[3] For a field in decline, DOR derives proven reserves from a decline curve based on the prior year's production.[4] Pipeline transportation property is also valued based on the estimated life of proven reserves, but DOR has the flexibility to use any standard appraisal method.[5] For its 2022 assessment, the DOR Tax Division's State Petroleum Property Assessor ("Assessor") applied replacement cost less depreciation based on proven reserves to all of Furie's property. DOR assessed the property at a full and true value of $81,747,510. Intervenor Kenai Peninsula Borough supports this assessment.

Furie has argued for an ever-shrinking full and true value. In its March 17, 2022 ICD appeal, Furie claimed the full and true value is $20,468,293. When it appealed to SARB on April 15, 2022, it claimed the full and true value is $18,153,468. By the time of the hearing one month later, however, Furie argued that the full and true value is $7,800,000.

II. DISCUSSION

SARB may adjust an assessed value that is unequal, excessive, or improper or that was not determined in accordance with AS 43.56.[6]

Furie argued that the assessment is excessive and improper because it exceeds the price HEX paid for the entire company in bankruptcy. Furie's argument would have SARB regard Furie's personal property as portion of the value of the entire enterprise. But the value of a company, with its obligations and liabilities, and the value of its personal property are apples and oranges. Furie is correct that a sales price, even in bankruptcy, can be relevant information in determining value. But not for how DOR determines value under its current regulations. DOR applies replacement cost new less depreciation based on proven reserves derived from the prior year's production. In Furie's most recent full and true value calculation, it used the same replacement cost as DOR, but continued to use the bankruptcy sales price as a basis for depreciation. That approach is not necessarily invalid, but it is inconsistent with the method DOR adopted by regulation in 15 AAC 56.100.

Furie also argued that the assessment is excessive because it failed to adequately account for Furie constructing facilities for greater capacity than it has been producing to date. The Assessor explained, however, that DOR's regulatory method for proven reserves depreciation

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2 15 AAC 56.100(a).
3 AS 43.56.060(d)(2); 15 AAC 56.100(a).
4 15 AAC 56.100(a)(3)(B).
5 AS 43.56.060(e)(2); 15 AAC 56.110(c).
6 AS 43.56.130(f).

captures the property's decreasing utility in the second step of the process. Furie did not demonstrate that DOR's application of this method resulted in an excessive assessment because of its facility capacity or utilization.

Furie argued that other factors led to an excessive assessment, but failed to support these factually. First, Furie claimed it pays a 25 percent royalty, twice the standard 12.5 percent royalty for Cook Inlet, and that this should be accounted for in the depreciation. But as its own exhibits specify, Furie pays the State only a 12.5 percent royalty. The other 12.5 percent is an overriding royalty interest ("ORRI"). An ORRI is ***not*** royalty. It is a percentage of gross production, free of costs, carved out of the lessee's working interest and paid to a third party, such as an investor or an assigning lessee who takes an ORRI in lieu of payment for assigning the lease.[7] How Furie chose to compensate investors or others should have no bearing on depreciation.

Second, Furie pointed to a Financial Assurances Agreement it entered with the State to create a sinking fund for eventual dismantlement, removal, and restoration ("DR&R") of its leases and argued this obligation should be accounted for in depreciation as a burden that is unique to Furie and not experienced by other producers in Alaska. Furie provided no evidence that its DR&R agreement is in any way atypical or unique.[8] Furie's DR&R obligations are certainly not unique; they are an obligation included in every State oil and gas lease. And as the Assessor explained, DR&R is a cost of doing business, not an aspect of proven reserves depreciation.

Third, Furie argued that Sterling reserves should no longer be considered proven reserves because of the challenges Furie has faced in producing from this interval. While Furie may have had trouble producing this gas, it did not demonstrate that it is no longer a proven reserve. To the contrary, Furie's own March 15, 2022 Production Analysis & Forecast included the Sterling and its witnesses testified that Furie has plans to test Sterling production this year. The standard specified in the statutes and regulations is "proven reserves," not easily produced reserves. Furie did not demonstrate that the Sterling is no longer a proven reserve for purposes of assessing the value of its property.

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[7] *Allen v. Alaska Oil & Gas Conservation Comm'n*, 1 P.3d 699, 700 n. 1 (Alaska 2000) (ORRI is "'a percentage of the gross production payable to some person other than the lessor'"); Williams & Meyers, Manual of Oil and Gas Terms at 792 (12th ed. 2003) (overriding royalty is "[a]n interest in oil and gas produced at the surface, free of the expense of production, and in addition to the usual landowner's royalty reserved to the lessor in an oil and gas lease.").

[8] To the contrary, the State regularly enters DR&R Financial Assurance Agreements like the one Furie submitted here, as explained in a March 11, 2020 letter from the Department of Natural Resources Commissioner to several legislators, available at https://dog.dnr.alaska.gov/Documents/PublicNotices/3-11-20_DRR_Primer_Final_06032020.pdf

DOR and KPB took issue with Furie providing evidence and analyses to the Board that it had not previously submitted to the Assessor, even going so far as to state that the Board should not consider such information. SARB's review is not based on a closed record like a court reviewing an administrative appeal. If it were, no party could provide facts to the Board and there would be no evidentiary hearing. That said, when SARB reviews information, it is through the lens of determining whether a burden has been met to show the assessment is unequal, excessive, or improper. In general, a taxpayer would be well advised to provide relevant information during the assessment and ICD process where the Assessor may consider the information without that lens. Here, the Board considered all information provided by all parties.

Overall, the evidence showed that DOR followed the applicable statutes and regulations when valuing Furie's property. Furie did not demonstrate that DOR treated it differently from other taxpayers. It did not show that the assessment is inconsistent with the law or otherwise improper. And despite raising many interesting issues, Furie did not demonstrate that DOR, in applying the methods set forth in statute and regulation, issued an excessive assessment.

III. CONCLUSION

As chair and on behalf of the State Assessment Review Board, and in accordance with AS 43.56.130(b), I certify to the Department of Revenue that the Board has determined that the assessed value of Furie's property on January 1, 2021 was correctly determined to be $81,747,510 and therefore Informal Conference Decision 22-56-01 should be affirmed.

DATED: May 20, 2022

James I. Mosley

James I. Mosley, Chair
State Assessment Review Board

Judicial review of this decision may be obtained by filing an appeal in the Alaska Superior Court in accordance with Alaska Rule of Appellate Procedure 602(a)(2) within 30 days after the date of this decision.

I certify that on May 23 2022, this document was served on the following by email:

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