

**ORAL ARGUMENT – 10/18/00**  
**00-0173**  
**COASTAL LIQUIDS V HARRIS CAD**

HUTCHESON: This is an ad valorem tax dispute regarding Harris CAD's listing an appraisal of the storage capacity within 6 underground salt dome caverns. The tax years are 1994 and 1995.

GONZALES: You described the caverns as natural characteristics to the land.

HUTCHESON: No. These caverns are made out of a salt formation.

GONZALES: Did Coastal spend money to change the characteristic of these caverns in order to prepare them for storage?

HUTCHESON: It's a little bit more complicated than that. Texas Brine is the outfit that actually runs the salt domes and brines salt. Essentially they mine salt out of this salt dome formation and sell it for commercial purposes. As a byproduct of that, a cavity is created in the salt formation. And the walls of that cavity are salt. And because of the characteristics of salt and the thickness of those walls, it's non-permeable. And, therefore, it's suitable for storage of...

HANKINSON: Was the money spent to make this space that was left suitable for storing the gas? Or could you just take the salt out and say that's it, now we can put gas in?

HUTCHESON: Absolutely. You could do that.

HANKINSON: But in this case?

GONZALES: Did Coastal spend money in this case?

HUTCHESON: No. Texas Brine created these caverns for their brining operations.

HANKINSON: But was money spent by Texas Brine or Coastal or somebody in order for this particular space that was created to be suitable for storing gas?

HUTCHESON: It was not created for the express purpose of creating a cavity suitable for storing gas. It was created by pumping water down into the formation, sucking out brine, and then selling the brine. That's Texas Brine's operation. The by-product is this cavity. Certainly money was expended to do that process.

HANKINSON: If they hadn't done that process, then you couldn't have stored gas in that space?

HUTCHESON: Absolutely. It would just be a soft dome formation.

PHILLIPS: Would the salt operation standing on its own be economically feasible?

HUTCHESON: Absolutely.

PHILLIPS: And there is no concrete spent to realign these walls or nothing \_\_\_\_\_?

HUTCHESON: Nothing at all. What the appraisal district is talking about if you think about it like a well...

O'NEILL: The appraisal district cites cases from other jurisdictions for determining that wells are structures. If that's the case, why isn't this a structure?

HUTCHESON: There's a difference between the equipment, the casing, the machinery and equipment associated with the actual brine process, the pumping in of water, the sucking out of brine and the hydrocarbon storage: how it gets down into the cavity.

O'NEILL: But isn't that the same as \_\_\_\_\_?

HUTCHESON: Yes. But in this instance the subject property is not that machinery and equipment. That's being separately appraised under another category. Additionally, all of the liquid petroleum product in the cavern is being separately taxed under the inventory or personal property of Coastal.

ENOCH: The casing and the cement that's down there in that hole is being taxed as personal property?

HUTCHESON: No. It's being taxed as machinery and equipment. But it's important to understand here the subject property before this court is the storage capacity, is the void within these caverns.

ENOCH: Let's assume that this property is a cave and somebody moves in with curtains, and dishwashers, and washing machines, and two beds and puts a front door on it. Is that an improvement or not?

HUTCHESON: Absolutely not.

ENOCH: So if I go over to some land and I carve out a ditch and I cover it with soil, and I have a manmade cave, is that an improvement?

HUTCHESON: No.

ENOCH: So people could avoid paying taxes on improvements on real estate if they just make their improvement out of the natural materials that are on the property?

HUTCHESON: Well they wouldn't avoid paying taxes if what they did to manipulate the land enhanced that land's value, then the land is worth more. But it doesn't make it an improvement.

HANKINSON: Do you disagree with this characterization this is what happened, that the construction of this hole in the ground included engineering and design, drilling a well bore, completion of the wells, solution mining and brine removal to develop the cavern, placement of casing and tubing within the cavern, cementing and installation of well head and pipeline equipment, and then the upper portions of the constructive cavern are cementing and then the walls are comprised of salt? Now all of that has to happen before you could store the gas.

HUTCHESON: Absolutely.

GONZALES: Why doesn't that transform the cavern into a structure or a fixture?

HUTCHESON: Because the definition of improvement under the Tax Code 1.04(3), specifically says that improvement is a building, a structure, a fence erected on or fixed to the land.

O'NEILL: That goes back to my original question. Other jurisdictions have interpreted an oil well to be a structure. Why isn't this a structure? Are you saying we shouldn't follow that case law?

HUTCHESON: No. I'm saying it's completely distinguishable. Wells and the rigging and the machinery and equipment associated with this salt dome storage facility are absolutely, separately taxable from the land. We're not arguing that. What we're arguing is the way the appraisal district did this is they figured out many barrels of brine were taken out. And these things are value based upon their capacity. How big they are. All of that value is associated with the land itself.

O'NEILL: If we were to go the other way, how would this property be taxed?

HUTCHESON: It would be taxed as the appraisal district has taxed the property in the year 2000, which is as a part of the land.

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HANKINSON: Mr. Ikard, did the CA's decision in this case substantially change the way taxing entities around the state of Texas have traditionally handled appraising these kinds of properties?

IKARD: Absolutely not.

HANKINSON: So all these amicus briefs that we have up here that say that all the school districts and counties have been taxing these things as an improvement are wrong, that hasn't been the usual practice in Texas?

IKARD: When this property that's the subject of this litigation was first placed on the appraisal roll in Harris county in 1994, it was placed on the appraisal roll as business inventory. So to suggest that these have been listed on the roll as improvements everywhere is just not correct.

HANKINSON: I just want you to respond to this whole big stack of amicus briefs that we have here that says that if we allow the CA's decision to stand in this particular case, that we will have substantially changed the practice of taxing entities throughout the state of Texas, and that we are going to be faced with this huge amount of taxpayer activity to recoup taxes that have been paid. Do you disagree with the amicus briefs, or do they correctly state the condition of things around the state with respect to this issue?

IKARD: There are certainly taxing jurisdictions, appraisal districts, that have listed storage capacity in salt dome caverns as improvements. There are also appraisal districts in Texas that have listed them as land. There are also appraisal districts in this state that have listed them as personal property, as business inventory. That's one of the reasons why we are here is because we believe it's a question of law that needs to be disposed of.

HANKINSON: I really want to know the impact of this decision. And so I take it by your answer then that you disagree with all the amici?

IKARD: What I agree with you is 1) that prospectively this will have absolutely no - we don't know what the impact is going to have prospectively, but certainly these caverns and the storage capacity in them will not escape taxation. That chicken little mentality just doesn't exist. The sky is not going to fall. Because whether they are listed on the appraisal roll as an improvement or they are listed on the appraisal roll as land as we contend, the value of them is still going to be subjected to property tax.

O'NEILL: Well if the value of them is attached to the land, then isn't the landowner the one who is going to be paying all these taxes as opposed to the person who is leasing it? These caverns are often sold rather than leased. What if you had bought this cavern, would it still be taxed with the land?

IKARD: What is being sold or leased is the storage capacity within the cavern. It's the void. And we think that that is a part of the land. But it can be separate. It can be transferred. And in this case for instance, Coastal has acquired it from Texas Brine...

O'NEILL: What if he had bought it?

IKARD: In this case, we would contend that the proper taxpayer would be the surface owner.

O'NEILL: Even if you had bought it?

IKARD: Even if we had bought it. On the other hand, in every instance that I am aware of, and certainly they are within the record in this case, the ultimate user of the property is contractually obligated to reimburse the surface owner for the taxes involved.

ENOCH: That includes the Methodist Church?

IKARD: Yes. That's taken care of contractually in virtually everything. It's like a tenant in a building having ad valorem taxes as an expense pass through.

ENOCH: Why are we even here?

IKARD: Because there needs to be...

ENOCH: I understood from Mr. Hutcheson that if you created a cavern, you made it into a home, that would enhance the value of the real estate. The taxes would be reflected in the real estate the surface owner pays. And you've just argued that under the contract if that circumstance occurred, then you would be responsible for paying for it. And if that's the case then, what difference does it make whether we say this is an improvement that's separately taxed, or it's not an improvement that's not separately taxed, but it can be factored in to the enhancement of the value of the real estate and so it's are going to be taxed.

IKARD: I believe that it's profoundly important and there needs to be a bright line drawn with respect into which category any real property assets subject to taxation in this state be placed. And the reason for that it's exactly as was discussed by this court in *Gifford Hill*, is the appraisal district in that case said, Well it doesn't matter what limestone rock is. It can be a mineral. It could be a miner quarry. It can be land. It doesn't matter how we list it. But writing for the court, Justice Hightower clearly pointed out that there were three reasons really why you need to figure out which category it fits. One is, to determine to avoid multiple appraisal, which we contend is exactly what happened in this case. Number 2, it is to make sure that property doesn't escape taxation which was the case in the *Credit Bank* opinion that we cited in; and in the *Walker* opinion we cited, where real estate was the category and the property owner attempted to argue that his improvements which were left off were subsumed within the real estate category. The court said, No. Improvements are separate. And thirdly, to determine the appropriate appraisal methodology to be employed with respect to that property. For instance in *Gifford Hill*, limestone rock if it's producing and inside a mine or quarry is appraised by the income approach. If it's not producing and it's outside the mine - it's part of the land - then it's appraised by the comparative sales analysis. And in that case there was a difference between \$800 per acre for land in Wise county containing limestone rock verses \$7.5

million for the miner quarry if the same rock were included within it.

ENOCH: Let's go into the quarry of the rock. If I understand the argument that is being made, if I carve out my living quarters from the limestone wall, then that's not an improvement to the property. Then my question is: Instead of carving it out of the wall, I just break the wall into separate pieces and go build me a wall out of that same limestone, how have we now defined the line that creates that as an improvement?

IKARD: I'm not as quick to answer that question as my colleague Mr. Hutcheson is. I think there could be situations which I can envision where sculpting out a residence from a limestone rock face could be considered an improvement.

ENOCH: Where is that line at?

IKARD: I think the line would be what you install there. For instance if all you do is dig a hole in the wall and nothing else, then I think that's not an improvement.

ENOCH: Suppose you carve out 3 walls, but you just put on 1 wall - a door - over the front?

IKARD: I think it's getting closer. And I think if you put a door on it it's getting closer. And I think certainly if you put electric wiring in it it's getting even closer. And if you start furnishing it with appliances it's getting closer.

In response to your question, let me just give you the best analogy I know. And that is, suppose we're in Alaska and a meat packing firm decides it needs some additional place to store its meat. And so there is a glacier in the back lot. And it goes out and injects hot water into the center of the glacier and creates a cavity. And then it goes out and it stores the meat in the cavity in the glacier until such time as demand requires the meat's usage. Well under the theory that the appraisal district has espoused in this case, that cavity in the glacier would be considered an improvement and then it would be put on the appraisal records as the most valuable and the largest commercial freezer in the US. I say that that melted cavity in the middle of a glacier is not an improvement.

ENOCH: If you put a door on it so you have access to and from, does that make it closer?

IKARD: No. In our case the injection and ejection wells, which Judge Hankinson was getting at and Judge Gonzales earlier, are taxed separately, the machinery and equipment and the piping in the building on the premises that are used to facilitate the storage of this product are listed separately on the appraisal rolls as machinery and equipment and improvements.

HANKINSON: Obviously if the cavern is considered part of the real property, then there is a particular appraisal method that is applied and taken into account the fact that there is a cavern on the real property, or is it not taken into account?

IKARD: The appraisal of the real property, you mean the surface, the land?

HANKINSON: If this cavern is not an improvement, in fact it's considered part of the real property, under the applicable appraisal method how does the existence of the cavern affect the value of the real property or does it at all?

IKARD: It does. And in fact,

HANKINSON: How does that figure in?

IKARD: Actually there have been numerous appraisals in this very case. And it is possible to go out and appraise property. In fact, we've done it where it is assumed that the storage capacity within the salt dome is part of the land. And you can actually see that land's transactions occur, which the land includes caverns for this purpose and so the value is enhanced substantially.

HANKINSON: But my point, which I think goes back to an earlier question, the cavern enhances the value of the real property. But apparently it does not enhance the value of the real property as much as the total value that would be attached to treating it as an improvement in valuing it, and then valuing the real property separately.

IKARD: Well, we don't know the answer to that question. Because in this case for instance originally the appraisal district put the storage capacities on at \$10 million. There was an appraisal which is attached to their papers that was presented by our people at our \_\_\_\_\_ hearing, which showed it was worth \$2 million. We now have appraisals to show that it's worth about \$600,000. There is the issue of how much this value enhancement is, is yet to be determined.

HANKINSON: But that's my whole point. Does it really make any difference or when you use the separate appraisal methods, do you end up at the same point because you are in fact considering the actual value of having the storage capacity and the economic value associated with it? Is there going to be a net difference to your client in terms of how much tax is paid, and to the taxing jurisdiction in terms of how much tax they receive?

IKARD: The answer is, we don't know. I think that's the only answer I can give you. I think though, you're going back to a question of whether or not there's going to be lost revenue as a result of this. And frankly, I don't think that's an issue that's relevant to the disposition of this case. Obviously in our court systems we instruct our jurors not to take into consideration the economic impact of their decisions. And I don't think this court should do that either. But I don't know the answer. I don't think anybody knows because so far not one of these cases involving salt domes has

reached the merits where the value of the salt dome, whether it's an improvement or whether it's subsumed within the value of the land has been determined.

HANKINSON: My reason for asking the question is I want to know why you all are fighting so hard over this if you don't think it really makes any difference. I'm trying to understand the impact of the issue in this case.

IKARD: That we're fighting over two issues: One is that as tax lawyers and our client as a corporate citizen believe that there is a fundamental legal right to have your real property characterized properly. So for two reasons: one, so the proper appraisal methodology will be employed; and two, so that you will not be put in jeopardy of multiple appraisal. We believe that as a matter of law the storage capacity in these salt domes in the Alameda facility was appraised twice for property tax purposes.

HANKINSON: Explain that.

IKARD: As we have stated in our briefs, if you conclude as a matter of law that this real property is not an improvement but it's merely a characteristic of the land, then if you conclude that as a matter of law, which we think you must, and 2) you agree with us that the Harris Co. appraisal district appraised as it is required to do that subject property at its fair market value, then if this property is also listed separately as an improvement, then that constitutes multiple appraisal as a matter of law. And it's just axiomatic.

O'NEILL: It does make a difference doesn't it in terms of being able to accurately appraise, because under your analysis you would have to use a comparable sales approach, which is almost impossible to do in a salt mine situation as opposed to appraising it as you would an over-ground storage tank or an underground storage tank which this would seem to have more similar characteristics to be more income \_\_\_\_\_.

IKARD: I disagree with your initial premise. It is not difficult to appraise salt dome formations which have storage capacity within them by the comparable sales method. We have commissioned and obtained several appraisals: 1) with respect to this very property; and 2) several with respect to other properties that are subject to the pending disputes. So, it is not difficult. It is done routinely. But the underlying concept that you are going at - the correct one - is that one of the reasons why it's important and why we're fighting to have the proper 1.04(2) category utilized is because that in part dictates the appraisal methodology. It's exactly what Justice Hightower said in *Gifford Hill*.

GONZALES: Going back to the property owner in Alaska. If that property owner spent millions of dollars to enhance the capacity of this cavern to freeze meat, would that constitute improvement?



IKARD: No. It may enhance the value of the land by however much money was invested in it. But it's still land. There was a semantics issue involved in the briefing in this case where the definition of improvement under 1.04(3) of the Code was dissected and each individual word definitions were used. But we just think this is common sense. In effect, the subject property in this case is nothing. It's just a void. It's air.

OWEN: When this was a salt dome, I assume that the minerals were taxed separately from the surface estate?

IKARD: The salt is appraised as land. It's not appraised as a mineral in place. Under the sections here, the salt is listed as land. It's not listed as a mineral in place, or it's not listed as mine or quarry for tax purposes. That's one of my biggest points that we raised in our briefs is that how can the void be an improvement but the salt walls be land? We think it's fundamentally inconsistent.

BAKER: You characterize this void as a nothing. And yet, you were willing to spend \$3 million to this void so you could use it. You don't consider that an enhancement in any way?

IKARD: No, I don't. It's a very interesting question. Because it directs the focus from an appraisal standpoint what you're looking at. In Texas, the value of property for property tax purposes is determined by value and exchange. It's what a willing buyer would give to a willing seller as everybody on the court knows. There's also another value standard which is called the "value in use", which is the value intrinsic to the owner of the property as if it were to be continued to be used the way it is. And obviously the value in use is much greater in this case. The value to Coastal is much greater than it would be to me. I can't use this as a storage facility. It has no value to me at all.

BAKER: Well even if you were the owner of the salt dome before Coastal came along, the fact that Coastal wants it enhances the value for use to you as the owner even though you don't have any intention of storing any material in there?

IKARD: That's true. And that would reflect - presumably there would be a universe of potential buyers out there who would have the capability of using it and it would be able to obtain the permits necessary to utilize it who would create demand for this property, which would enhance the value of the land under which the salt dome exists.

O'NEILL: If you had bought this cavern instead of leasing it, I'm not sure I understood your answer to my last question. You're saying it would still be taxed to the surface owner even though you owned it?

IKARD: It is our contention that it would be taxed - I misspoke because I think I misunderstood your question. The owner of the property would be ultimately liable for the taxes on

it. But it would still be land. It would just be a part of the land which has been severed from the surface.

O'NEILL: You would pay the taxes on it and you would seek reimbursement from the landowner?

IKARD: Perhaps. Perhaps not. That would have to be determined by contract between us. It would not be within the province of the taxing authority to make that \_\_\_\_\_.

O'NEILL: If you just bought it outright: I'm going to pay you X amount of money for these salt domes and there is nothing said about it, how would that work?

IKARD: If what you're saying is that if Coastal goes and says I want to purchase the storage capacity within this cavern, then it would be the taxpayer. At the end of the day on Jan. 1, the value of that storage capacity would be placed on the appraisal roll in the name of Coastal Liquids Transmission LP as land. And it would be valued accordingly. That's how we believe it should be valued.

OWEN: You can sever the surface from the salt dome?

IKARD: Yes.

OWEN: And you can sell them and own them separately?

IKARD: Yes.

OWEN: And so why can't they be taxed separately?

IKARD: They can be taxed because an improvement is a separate entity of real property that has value in and of itself.

OWEN: It may be taxed as real property but you can sever the surface from the dome?

IKARD: Right. The important difference here is that the value of the land is to say the using of pie is a - there's a 100% value to the unsevered land. All of the characteristics that contribute to the value of the land constitute 100% of its value. If you sever a portion of that and cut it out in the form of this storage capacity, part of that value will now be assigned to Coastal for the purposes of determining property tax value. But the 100% of the value of that land has to set the upper limit of the value of the whole. But if the land account is here and the improvement account is over here, then you can have the land account setting one upper and then the improvement can have no upper limit to its value whatsoever.

OWEN: When a salt dome is being mined how is that taxed?

IKARD: The salt deposit that is unproduced, it hasn't been removed from the ground yet is land. And then as it is dissolved and ejected from the dome in the form of brine, it is taxed as business personal property. It's inventory.

OWEN: It's taxed as land as opposed to a mineral?

IKARD: Yes.

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RESPONDENT

ENOCH: There's been a lot of questions about whether this is an improvement or not. But you have raised a question in your briefs about the authority of Coastal even being in court. It is not clear to me in the briefing - segregate from the 1994 decision taxes and the 1995 decision taxes. What do you claim was wrong with their registration as a formed corporation and did you make that complaint to both their suing over the 1994 taxes and the 1995 taxes \_\_\_\_\_?

DELL'OSSO: The appraisal district complained about it on both years. There was a verified pleading which alleged that Coastal was not registered in Texas with the Secretary of State, and it stated for 1994 and 1995. That allegation was carried forward through all the briefing in the TC on up to the CA.

ENOCH: And who has the burden to establish whether or not they were registered?

DELL'OSSO: The appraisal district.

ENOCH: If the record is unclear as to whether or not they had properly registered in 1995, would the district lose on that \_\_\_\_\_ as to 95?

DELL'OSSO: Not under the record as it exist in this case. I think it's perfectly clear that it was alleged from day one that they were not registered with the secretary of state until 1995 in compliance with the limited partnership act, sec. 907A. And the contents of that act make it clear they have to meet all the requirements of it.

ENOCH: Which includes paying all of the fees.

DELL'OSSO: Right.

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REBUTTAL

HUTCHESON: The record reflects if you will that the surface owners are going to be reimbursed for taxes. That's an important point. The record does not reflect that. There is nothing in the record about that. In this case what the record does reflect is that the surface land, at least as to 3 of the 4 tracts which overly the caverns, are severed. The appraisal district simply cannot appraise as a characteristic of those three owner's land these caverns. These are valuable improvements under any definition that's applicable.

HANKINSON: Does the CA's decision in this case as the amici urged represent a departure from the practice of taxing jurisdictions around the state of Texas with respect to salt domes?

HUTCHESON: The record doesn't reflect the...

HANKINSON: I understand. But the amici have brought that issue to our attention. I just want to know if that's your view that we're looking at a substantial change in the way taxing jurisdictions handle this kind of an issue if the CA's decision is allowed to stand?

HUTCHESON: Yes. Not just on this kind of property. That's a real problem with this decision in this case. It allows multiple appraisal to be established based on bald assertions. If there was a multiple appraisal in this case it would have been a simple matter to point that out.

HECHT: Well you did tax the land.

HUTCHESON: Yes.

HECHT: And if their position is right that this should have been included in it presumably you didn't include it in there.

HUTCHESON: There is no evidence in the record that there was any listing an appraisal of these storage caverns.

HECHT: Do you tax it as land now?

HUTCHESON: That's not in the record. I think I can say this legitimately. Obviously with the decision at hand, the appraisal district has been steered in a particular direction. It has no choice until it gets some relief from this court.

HECHT: What difference does it make as long as you can tax both? Address the questions that we asked your opposing counsel here. What difference does it make to the appraisal district whether you tax it as an improvement or as land?

HUTCHESON: It makes a substantial difference. In this case at hand for example just to use it, the case on point, the land is severed from the caverns. So the district is not at liberty again to tax

those caverns as a characteristic of these other three landowners' property.

OWEN: You can tax separately as land surface ownership and mineral ownership. Whether it's severable or not doesn't have anything to do with whether you tax it an improvement or as land does it? You can tax separated property ownership as land. Both as land. So what does severance got to do with it?

HUTCHESON: Severance has to do with in any case and any property of this type or similar property, the property can be analyzed and analogized to it in any way. The appraisal district could not tax...

OWEN: You tax minerals as land even when they are severed from the surface. Why couldn't you tax these salt domes as land even when they are severed from the surface? Tax them as a mineral interest, as real property, even though the interest is separated from the surface. Why aren't they still real property for tax purposes severed or not?

HUTCHESON: These caverns are substantially improved to the extent that they are improvements...

OWEN: That begs the question. Why couldn't you tax them as real property for whatever their value is?

HUTCHESON: I don't believe under the state of facts in this case that the appraisal district is at liberty to decide that those should be taxed to the land and not listed as improvements. Furthermore, it's a real quandary. Here you are faced with a case that alleges a multiple appraisal that the appraisal district says didn't occur. Whereas, if you had land in the same account even, land and improvements, obviously there wouldn't be any question that there was no multiple appraisal. So we would want to put improvements, in this case, structures of this type into a separated category of improvements.

OWEN: But as long as you are taxing the overall value, what difference does it make to you which category you put it in as long as the value is captured?

HUTCHESON: I believe that the argument could be made against the district that if we had to break them out as improvements, that we could have lumped them into the land, that they couldn't be appraised as part of the land. There was a statement made for example to illustrate that point, that there is appraisals in the record that indicate that these caverns have been assumed to be land or were appraised as land. And that is not correct. There is three appraisals in the records that each of them appraised these caverns separately.

OWEN: How are they appraised in condemnation proceedings?

HUTCHESON: I can't answer that.

HECHT: If we say these structures have to be appraised as land from this day forward, are you going to be able to do that?

HUTCHESON: I would imagine we would have to do that. Yes.

HECHT: Will it make any difference to you whether there is land or improvements from the standpoint of whether you are going to get the revenue?

HUTCHESON: Not from a revenue standpoint. And that's not what this is about. But if you have a circumstance that you have here again where there is a severance between the cavern and the surface, then it's hard to visualize how the district could appraise those as land.

ENOCH: On this land that exist out there, you have as raw land out there and do you apart from minerals, which you are allowed to tax anyway, would you be able to tax assuming there wasn't a severance of this salt dome, would you be able to tax the surface owner for what geological formations exist below the surface that are not minerals in place? Could you tax them for limestone or shells or gumbo or something that exists under them because there might be a commercial market for that if they ever decided to open it up as a mine?

HUTCHESON: No. I believe that question has been answered by *Gifford Hill*, where it held that limestone is part of the land. But in that case, this court...

ENOCH: But when you say it's part of the land, that's my question. If it's part of the land, does that mean that you can look at comparable vacant land out there and then add a factor to the value of that land because it also has some sort of shell or some sort of geologic formation underneath it that might have some commercial value for it?

HUTCHESON: If it's taxable under the tax code it could be added. We wouldn't add up all the different components of what might lie under there otherwise, and then value that as land.

O'NEILL: If you tax them as land it can yield a lower value on a comparable sales approach as opposed to if you value them as improvement. Doesn't that look more at what income the property produces? Isn't that what we're fighting over? I mean if the appraisal is going to be the same under either method, I'm not sure what we're fussing about.

HUTCHESON: There would be three different ways to appraise it. But all the evidence in this case shows that how these caverns are appraised is separately. Now whether you value the land, an appraiser does, and then values the caverns, and adds those two together, you still appraise the caverns separately.

PHILLIPS: Won't there be different tax rates if the surface is subject to various exemptions you're having to pay? The appraisal number may be the same, but might the rate not be different?

HUTCHESON: No. It wouldn't be different on the different category of the property. In fact in *El Paso CAD v. Montro Partners* has a quote in it that talks about that. It says it's not the appraised value that's in issue. It's the underlying item that's being taxed.

The agricultural exemption did apply to everything that was under the land except that part that was in the quarry. So this decision out of the First CA leads us to argue that in the future how that's going to relate to agricultural exemptions and how it will relate to that exemption as to any profile if you will of that cavern that's under the land.

ENOCH: Coastal argues that they have the authority as an agent or lessee under a later statute in 1995 to come into court to handle this appraisal dispute and they argue that that is a more specific statute than the statute that requires them to register as a limited partnership to come to the court. How do you respond to that argument?

HUTCHESON: I disagree that they make that specific argument. But I will answer the question follows the prohibition against maintaining an action, suit or proceeding in Texas would apply to any statutory or other cause of action. It doesn't exclude code provisions, this code or any other code. So it's not trumped. Limited partnerships don't enjoy any greater rights than anyone else who has a right under any other code or statute. In this case, the limited partnership is prohibited under 907A from maintaining an action, suit or proceeding in Texas till it was properly registered.

In *Enterprise Products Co. v. Board of Supervisors of the Forest County and the Petals School District*, 729 Southern 2<sup>nd</sup>, 790. In that case, the Mississippi Supreme Court referencing an AG's opinion (930328) in that state, addressed caverns just such as these as improvements under their code that are separately taxable from land. The appraisal district contends that under the definition of improvements that these fit clearly within the definition of structure. Of course, definition of improvements says a building structure, a fixture fence, direct owner of fixed land. Because these are manmade structures, they are improvements under the plain meaning, common usage of those terms.

GONZALES: At what point does something like this become a structure? What would someone like Coastal have to do or stand in order to make something that's natural into a structure? Could their use turn something natural into a structure?

HUTCHESON: Use, possibly. That would be a harder one to imagine. In this case there was substantial amounts of money as reflected in the RR Commission records that are in the record and in the appraisals that reflect there was a substantial amount of money and substantial improvement to the property in the form of a cement in the upper portions of the cavern. They are sealed off. A

wellhead is put on them. They are connected to pipelines. So you get away from whether it's just used for something. For example: a hole in the ground that might be used to store something, where you can walk over and drop a rock in it, that's not the case here at all.

GONZALES: But how does a county determine whether or not something becomes a structure and thereby an improvement? What would Coastal have to do to make it - what is the minimum amount of money spent or activity by Coastal that would turn this natural characteristic of the land into a structure?

HUTCHESON: Well within the definition of structure, at the point that they had joined together parts to outfit, whatever this thing we're talking about is for a particular use and to give it that utility. It's the act of putting the parts together, joining component parts together that make it a structure.

GONZALES: So if they attach some little thing to this natural characteristic, and that would have transformed this natural thing into an improvement because it's a structure now?

HUTCHESON: One attaching, one point might not. I wouldn't argue that.

HANKINSON: What is the economic impact of the CA's decision in this case? We've kind of asked it in several different forms, and I don't think I still figured out yet why it makes much difference in whether or not it means that less taxes will be collected in substantial amounts, whether property will escape valuation. I'm not really sure. What is the economic impact of the CA's decision in this case?

HUTCHESON: You've alluded to the matters before you there in those other briefs. But as far as whether it's in one place or another place?

HANKINSON: Yes.

HUTCHESON: They should be substantially the same numbers.

HANKINSON: Then why do we have all of these amici saying that the world is going to come to an end if we let the CA's decision stand and that all this property is going to escape taxation?

HUTCHESON: Without addressing the amici, what this case stands for is propositions on balled assertions of multiple appraisals. We have no other case in Texas that has ever allowed that to happen. Whether it was just a balled assertion that multiple appraisal has occurred, persons can now come in and argue descriptions and what's been added or use, or a variety of things which your questions have touched on today and say just because of this misdescription, we now have a multiple appraisal. So from that standpoint alone the prohibition if you will by the opinion of the appraisal district appraising what can be legitimately characterized as improvements could be huge. Not to



mention what it would do in terms of litigation, or will do in terms of litigation.

O'NEILL: So you don't really care so much whether it's taxed as improvement or as land as long as it's not considered a multiple appraisal?

HUTCHESON: I was addressing the circumstance where people do come in and address it as a multiple appraisal. And what that leads to...

O'NEILL: Does it matter to the appraisal district whether it's characterized as improvement or land just as long as in this instance we don't call them multiple appraisals? You really care.

HUTCHESON: No, we really do care.

O'NEILL: Why?

HUTCHESON: Not withstanding the question, the fact that it's been severed we are constrained and cannot appraise as a characteristic of the land these caverns are someone who don't own them. And that can happen in other places in the state as well as here.

GONZALES: Going back to Justice Owen's question: Why can't you just because it's been severed tax them as land just because they've been severed?

HUTCHESON: You're suggesting we would have two land accounts, one going to party A and one going to party B?

GONZALES: I don't know. Is that why, because administrative burden or...you say you can't do it. I just don't understand why.

HUTCHESON: Well I can obviously see that there would be an argument there that you can't appraise land twice. That's the argument that would be made I think in that fact situation.

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HANKINSON: Mr. Ikard, earlier in response to one of my questions, you said that we should not concern ourselves with economic impact. I just want to ask you one more time. Do you want to stand on that or do you want to talk to us about that?

IKARD: I would like to stand on it, but I won't. First of all, I think that Mr. Dell'Osso gave the correct answer when he said prospectively that there probably won't be any revenue impact. The question that is raised by the amici is whether or not folks who are the owners or operators of similar properties located in other jurisdictions, properties which have been listed as improvements

will attempt through what's known as a section 2525(c)(3) motion to go back in time 4-5 years depending on how you interpret the statute to argue that there was multiple appraisal. Because that's one of the three conditions under 2525(c)(3) that allows you to go back to correct the appraisal roll after the statutory period. So in the event those folks are successful - let's assume that you determine this is land, the amici are saying that the floodgates will open and there will be hundreds of these salt dome operators who will file 2525(c)(3) motions, and then there will be a concomitant reduction in the tax base by however many zillions of dollars they've postulated in their briefs, which of course, isn't in the record and there's no substantiating of any of those dollar amounts they quoted.

But it's our position that sure if there was multiple appraisal, it's illegal and there shouldn't have been. And that unlawful conduct on the part of the appraisal districts would have to be redressed. But I don't know what the result is going to be. They are going to have to take the step - you're going to have to determine its land. They are going to have to take the step of filing a 25.25(c)(3) motion. The appraisal review board is going to have to deny that. It's going to have to go up to the courts and then there is going to have to be a determination of whether there was in fact multiple appraisal, which there may not have been as a matter of law.

OWEN: You say multiple appraisal, but isn't really the question is whether they put - if they put it in the category improvement and therefore put most of the value in improvement category as opposed to land value, and improvement we say, No it's not an improvement. They can't go back and revalue retrospectively and put the value back in the land category. Isn't that what really happened in this case?

IKARD: Not really. It's close. What this amounts to is you need to assume that the value of the land in its totality with no interest severed from it is X. And then if a portion of that land, a characteristic of that land is separated out and called something else, an improvement in this case, and its value Y, and there is not a simultaneous adjustment in the value of the land account downward to reflect the taking out of the other piece of the property, that is that the land account stays the same but there is another account that is associated with the value of the other asset, then that asset has been appraised twice.

OWEN: But we don't know one way or the other. The amici you're complaining about is they may have put most of the value in the improvement category as opposed to the land category.

IKARD: But that's for the amici to figure out. If you're talking about those other cases that Justice Hankinson was talking about, that's to be determined on a case-by-case basis as they arise. In this case, we're saying - we know as a matter of fact and it is in the record that these salt storage facilities were not listed separately on the appraisal roll in 1993. They were in operation from 1981 through 1993, but they weren't separately listed, and the value of the land account in 1993 was X amount of dollars. In 1994, all of a sudden these salt dome storage facilities appeared on the appraisal roll at a value of \$10 million. The land account in 1994 stayed the same. It didn't change from 1993.

ENOCH: For the 1994 appraisal, you argued that you were designated as the agent in the lease to represent Bryan in the tax protest, and you come up here. And to that the appraisal district has argued because you are not registered as a limited partnership, you cannot come into court to do that. You have not really had an opportunity to talk about that, but if the court concludes that even the designation in the lease agreement whether it was timely or not filed timely, how do you - what gives you the authority to come into court when in 1994 you weren't registered as a limited partner \_\_\_\_\_?

IKARD: That's the peril dividing the argument. My associate, Mr. Hutcheson was supposed to talk about all those issues concerning standing and I don't think he addressed one minute's worth of it. In short form to specifically answer your question, is that §9.07(b) of the Texas Revised Limited Partnership act states that the failure to register does not impair defense. So our position is that because...

ENOCH: We have 4209 that says defense does not impair your defense in court?

IKARD: Correct.

ENOCH: But you filed the lawsuit.

IKARD: That's correct.

ENOCH: To win on that point, essentially to overturn the decision in 1994, you have to win on the point that this really is a defensive posture that you're in and that you ought to be allowed to appear?

IKARD: Yes.

ENOCH: And for 1995, Coastal registered mid-way 1995 but the record is unclear as to whether they paid all fees necessary. So for 1995, to maintain against their complaint, their challenge, to maintain that judgment the court still has to also conclude that this was a defensive posture?

IKARD: That's correct.