Private Letter Ruling No. 04-003
Redacted Version
September 2, 2004
Severance Tax

Deduction of Transportation Costs from Value of Oil and/or Condensate

This is in reply to your request, on behalf of your client (taxpayer), for a private letter ruling with respect to issues concerning oil production and pipeline transportation in *Area X*, offshore Louisiana, in the Gulf of Mexico, for the time period *mm/dd/yy* (the pertinent time period), through the date of your letter. A plat (*Exhibit A)* supplemented your request. The private letter ruling applies only to the taxpayer and is based upon and limited strictly to the facts stated below.

Facts

You provided the following facts:

- Taxpayer is engaged in oil and gas exploration and production in *Area X* of the Gulf of Mexico.
- Taxpayer's Gulf of Mexico operations include exploration and production activities offshore Louisiana.
- *Exhibit A* is a plat depicting the extensive pipeline transportation system that taxpayer used to transport oil and gas from wells in *Area X* to distribution facilities outside of taxpayer's lease block.
- Highlighted on *Exhibit A* are the lease boundaries for taxpayer's areas of production.
- Contained within the lease boundaries are numerous wells and production platforms.
- The production platforms are connected to gathering pipelines.
- This intricate gathering line system is contained within the lease boundaries for taxpayer's areas of production.
- Taxpayer owned, maintained, and operated the gathering pipelines.
- The gathering system is set up such that all gathering lines for oil are directly or indirectly connected to one of two central accumulation points, Platform *Y* or Platform *Z*,
- At each of these central accumulation points, the oil is treated or processed, making it pipeline quality.
- At each of these central accumulation points, the oil then enters a 10" transportation line that is wholly owned, maintained, and operated by the taxpayer.
- The transportation lines transports the oil to terminals located outside of taxpayer's lease block.

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- At the two off-lease terminals, the oil is then tied-in to pipelines, at which point the oil is sold.
- The taxpayer does not sell the oil until it reaches the export tie-in terminals.
- Taxpayer did not own or operate the pipelines located at the tie-in terminals.

Ruling Requested

Taxpayer requests that the Department of Revenue issue a private letter ruling, which states that the gathering and transportation pipeline system utilized by taxpayer during the pertinent time period in *Area X*, as depicted on Exhibit *A*, entitles taxpayer to take the $0.25 per barrel deduction for all oil produced in *Area X* and transported through that pipeline system.

Discussion

The provisions of L.A.C. 61:I.2903 define how the value of oil and/or condensate is to be computed for severance tax purposes. With respect to deduction of transportation costs from the value computed, L.A.C. 61:I.2903(A)(h) provides as follows

> h. T*ransportation Costs* there shall be deducted from the value determined under the foregoing provisions the charges for trucking, barging, and pipeline fees actually charged the producer. In the event the producer transports the oil and/or condensate by his own facilities, $0.25 per barrel shall be deemed to be a reasonable charge for transportation and may be deducted from the value computed under the foregoing provisions. The producer can deduct either the $0.25 per barrel or actual transportation charges billed by third parties but not both. Should it become apparent the $0.25 per barrel charge is inequitable or unreasonable, the secretary may prospectively redetermine the transportation charge to be allowed when the producer transports the oil and/or condensate in his own facilities.

A "producer" is any person engaging in the business of oil or gas production, including the owning, controlling, managing, or leasing of any oil or gas property or oil or gas well capable of producing oil or gas or both.

As contemplated by the regulation, the phrase "own facilities" means that the pipelines, trucks or barges used to transport the oil and/or condensate are owned or operated by the producer. The producer is considered to be the owner or operator of pipelines, trucks, or barges used by the producer to transport oil and/or condensate when the producer has direct, immediate, and exclusive authority over such pipelines, trucks or barges

The word "transportation" is used in the regulation in its ordinary sense and comprehends a substantial movement of oil, after gathering, by pipelines, trucks or barges. Thus, movement of crude oil by gathering lines or other related equipment primarily used to produce, gather, or transport crude oil from the well to a point where it can be treated or processed to make it pipeline quality is not the "transportation" of oil as contemplated by the regulation.

The $0.25 per barrel deduction is deemed to be a reasonable charge for transportation costs when the producer transports oil and/or condensate in his own facilities. Reasonable or equitable costs of transportation are costs that are fair, proper, or moderate and are ordinary and necessary expenses incurred by the producer to transport the oil and/or condensate in his own facilities after gathering. The reasonableness or equitableness of the $0.25 per barrel transportation charge is a question of fact and involves a case-by-case consideration of all the facts and circumstances of the particular case under review.

Thus, a producer of oil and/or condensate is entitled to take the $0.25 per barrel charge from the value of the oil and/or condensate computed in accordance with the provisions of L.A.C. 61:I.2903 only when the producer (1) transports, i.e., substantially moves, oil and/or condensate by pipelines, trucks, or barges that are owned or operated by the producer, and (2) the $0.25 per barrel charge is equitable and reasonable under the facts and circumstances of the particular case under review.

Ruling

With respect to the two transportation lines, it is determined that the taxpayer transported oil in his own facilities as contemplated by the regulation. Therefore, the taxpayer is entitled to deduct the $0.25 per barrel charge as reasonable and equitable transportation charges from the value computed under the provisions of L.A.C. 61:I.2903 for all oil that the taxpayer transported through the two 10" transportation lines to terminals located outside of its lease block and sold during the pertinent time period.

Gathering lines neither constitute the taxpayer's own facilities nor transport oil as contemplated by the regulation. Therefore, the taxpayer is not entitled to deduct the $0.25 per barrel charge for any crude oil gathered and moved by the taxpayer's gathering lines from the well to the two central points of accumulation where such oil was treated and/or processed to make it pipeline quality.

Sincerely,

Cynthia Bridges
Secretary

By: Annie L. Gunn
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Policy Services Division

A Private Letter Ruling (PLR) is issued under the authority of LAC 61:III.101.C. A PLR provides guidance to a specific taxpayer at the taxpayer's request. It is a written statement issued to apply principles of law to a specific set of facts or a particular tax situation and is limited to the matters specifically addressed. A PLR does not have the force and effect of law and may not be used or cited as precedent. A PLR is binding on the Department only as to the taxpayer making the request and only if the facts provided with the request were truthful and complete and the transaction was carried out as proposed. The Department's position concerning the particular tax situation addressed remains in effect for the requesting taxpayer until a subsequent declaratory ruling, rule, court case, or statute supersedes it.