True Oil Co. v. Commissioner, 107 T. C. 119 (1996)

A formal well-category determination under NGPA section 503 is required to qualify for the nonconventional fuels tax credit under section 29.

Summary

In True Oil Co. v. Commissioner, the court addressed whether a well producing from a tight formation must obtain a formal well-category determination to qualify for the section 29 nonconventional fuels tax credit. True Oil Co. , as tax matters partner for Nielson-True Partnership, claimed credits for gas produced from the Hanson well, which lacked such a determination. The court held that a formal determination under NGPA section 503 is necessary, emphasizing the statutory requirement for a determination in accordance with NGPA procedures. This decision impacts the eligibility for tax credits for gas produced from tight formations, requiring strict adherence to regulatory processes.

Facts

True Oil Co. and Nielson Enterprises, Inc. formed Nielson-True Partnership to drill wells in the Wattenberg Field's "J" Sand formation, producing gas from tight formations. The partnership claimed section 29 tax credits for 1991 and 1992 for gas from the Vonasek and Hanson wells. The Federal Energy Regulatory Commission (FERC) had determined the Wattenberg Field to be a tight formation, and the Vonasek well received a well-category determination from the local regulatory authority. However, the Hanson well did not have such a determination due to an oversight. The IRS disallowed the credits for the Hanson well, leading to the dispute.

Procedural History

The IRS issued notices of final partnership administrative adjustment to True Oil Co. , disallowing the section 29 credits for the Hanson well. True Oil Co. contested the disallowance, leading to the case being heard by the U. S. Tax Court. The court's decision was the first to address the necessity of a formal well-category determination for the section 29 credit.

Issue(s)

1. Whether a well producing gas from a tight formation must obtain a formal well-category determination under NGPA section 503 to qualify for the section 29 nonconventional fuels tax credit.

Holding

1. Yes, because section 29 requires that the determination of whether gas is produced from a tight formation be made in accordance with NGPA section 503

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procedures, which include obtaining a well-category determination.

Court’s Reasoning

The court interpreted the statutory language of section 29, which mandates that the determination of tight formation gas be made in accordance with NGPA section 503. The court found the term “determination” unambiguous, requiring a formal process as outlined in NGPA section 503, which includes a four-step procedure for obtaining well-category determinations. The court rejected True Oil Co. ‘s argument that the legislative history and context suggested a different interpretation, emphasizing that the plain language of the statute required a formal determination. The court also noted that the legislative history of subsequent acts, such as the Natural Gas Wellhead Decontrol Act of 1989, did not change the requirement for a formal determination. The decision was supported by the court’s adherence to the plain and ordinary meaning of statutory terms and the consistent application of NGPA section 503 procedures for both price incentives and tax credits.

Practical Implications

This decision clarifies that producers seeking the section 29 nonconventional fuels tax credit must strictly adhere to the NGPA section 503 procedures, including obtaining a well-category determination for each well. This ruling impacts how similar cases are analyzed, requiring a focus on procedural compliance rather than just the physical characteristics of the well. Legal practitioners must ensure clients follow these procedures to secure tax credits. For businesses, this decision underscores the importance of regulatory compliance in claiming tax incentives. Subsequent cases have reinforced this requirement, ensuring that the procedural aspect of NGPA section 503 remains central to eligibility for the section 29 credit.

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