No. 13-1216

In the Supreme Court of the United States

MISSOURI GAS ENERGY, ET AL.,
Petitioners,

v.

STATE OF KANSAS,
DIVISION OF PROPERTY VALUATION,
Respondent.

On Petition for Writ of Certiorari
to the Supreme Court of Kansas

BRIEF IN OPPOSITION

WILLIAM E. WATERS
Special Assistant
Attorney General
Division of Property Valuation
Kansas Department of Revenue
Docking State Office Building
4th Floor
915 S.W. Harrison Street
Topeka, KS 66612
(785) 296-4035

DEREK SCHMIDT
Attorney General of Kansas
STEPHEN R. McALLISTER
Solicitor General of Kansas
(*Counsel of Record*)
JEFFREY A. CHANAY
Deputy Attorney General
BRYAN C. CLARK
Assistant Solicitor General
120 S.W. 10th Avenue
2nd Floor
Topeka, KS 66612
(785) 296-2215
steve.mcallister@trqlaw.com

Counsel for Respondent the State of Kansas

Becker Gallagher · Cincinnati, OH · Washington, D.C. · 800.890.5001

QUESTIONS PRESENTED

Petitioners' Question Presented fails to identify clearly the two legal questions the Kansas Supreme Court actually decided in rejecting petitioners' Dormant Commerce Clause challenge to the Kansas taxation system. The two questions properly presented for this Court's possible review are as follows:

1. Whether the "bright-line" rule of *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), that requires a "physical presence" by the taxpayer in the taxing jurisdiction applies outside the context of sales or use taxes; specifically here, whether that rule applies to ad valorem taxes which by definition apply only to property physically present within the taxing jurisdiction's borders?

2. If the answer to the previous question is negative, then the second question is whether the Kansas ad valorem tax on natural gas being stored in Kansas is valid under the four-part test of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977)?

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

STATUTES

RULE

OTHER AUTHORITY

FACTUAL STATEMENT

Introduction

Petitioners ask this Court to review a decision of the Kansas Supreme Court that is entirely consistent with the only decision of another state court of last resort to address the questions presented. Moreover, petitioners offer a distorted characterization of how the interstate natural gas pipeline system operates.

Petitioners effectively argue that Kansas cannot impose ad valorem taxes on *any* gas stored in the state because Kansas cannot identify the owner of any "specific molecules of gas transported through or stored in Kansas," which petitioners concede would be "impossible" to do. Pet. 2. Petitioners' track-the-molecule theory, however, is disproven by its own logical implications. Under this theory, petitioners would have to ensure that they withdraw the same molecules from the pipeline at point B that they delivered to the pipeline at point A, or else they could be taking and using someone else's natural gas. That result would be absurd, as petitioners agree. *See id.*

Petitioners also emphasize that they "have no control over—nor any knowledge of—the routing or location of their gas." Pet. 2. That may be true, but petitioners signed transportation and storage contracts with pipelines with storage facilities in Kansas. Under those contracts, petitioners retain title to gas in the pipeline, receive a right to withdraw an amount of gas equal to the amount they tender to the pipeline, and they agree (as they must under federal regulations) to an allocation of the pipeline's stored gas for purposes of state ad valorem taxes. Petitioners also reap significant financial benefits from the pipeline storing gas in Kansas.

Petitioners Have A Substantial Connection With Kansas—A Share Of The Natural Gas That Pipelines Store In Kansas.

Petitioners are non-Kansas public utilities that contract with interstate pipelines to transport and store natural gas they purchase from producers and marketers across the country. Pet. 6a. Petitioners purchase the gas, deliver it to a pipeline, and then designate when and where to take delivery of their share of gas from the pipeline. *Id.*

Once in a pipeline, petitioners' gas becomes commingled with other gas in that pipeline. Pet. 7a. No one attempts to track whether petitioners receive the same molecules of gas they put into the pipelines; the gas in the pipelines is fungible and petitioners do not control where it is transported or stored. *Id.* at 6a, 48a. But petitioners always retain title to "their" gas. The pipelines never acquire title to the gas; ownership remains vested in petitioners. *See, e.g.*, *id.* at 102a, 135a, 146a, 156a, 168a; *see also id.* at 53a (under federal regulations, petitioners retain title to gas they deliver to a pipeline and own gas stored in a pipeline's storage facilities). And petitioners always retain a contractual right to withdraw "their" gas, *i.e.* an amount of gas equivalent to what petitioners delivered to the pipeline. *Id.* at 7a.

Four interstate pipelines—Northern Natural Gas Company, Panhandle Eastern Pipe Line Company, Colorado Interstate Gas Company, and Southern Star Central Gas Pipeline—not only transport petitioners' gas from point A to point B, but also store petitioners' gas in underground storage facilities in Kansas. Pet. 7a; *id*. at 63a-64a (finding that petitioners' natural gas is stored in underground formations in Kansas). Underground storage serves several purposes beneficial to petitioners, specifically the following: (1) allowing petitioners to stockpile gas during off-peak seasons when prices are lower; (2) allowing petitioners to defer delivery of gas until it is needed (generally driven by weather-related fluctuations in consumer demand); and (3) allowing petitioners to deliver gas at one location and receive gas at another location simultaneously. *Id.* at 6a-7a; *see also* Am. Gas Ass'n Amicus Br. at 10.

Petitioners might not know the "specific … location of such storage" and may not be able to "designate a particular location for … storage." Pet. 4. But it was no secret to any of the petitioners that the four pipelines at issue in this case have storage facilities in Kansas and that petitioners would be allocated a share of the gas stored in Kansas. *See id*. at 76a-77a, 89a, 97a, 109a, 118a-119a, 129a-130a, 142a, 152a, 161a-162a, 173a-174a (by contract, and consistent with federal regulations, some of the gas purchased by petitioners is designated as being placed into storage by the pipeline for withdrawal on a seasonal and scheduled basis); *see also id.* at 19a-20a (quoting with approval Oklahoma Supreme Court's conclusion that because MGE contracts for storage knowing that an Oklahoma facility is one of the pipeline's storage facilities, "MGE cannot claim it does not intend for" its gas to be stored there).

Moreover, when petitioners contracted with these pipelines, petitioners agreed to a Federal Energy Regulatory Commission (FERC) tariff that allocates to the pipelines' customers a share of the pipelines' stored gas for purposes of paying state ad valorem taxes. Pet. 4a-5a, 47a. The FERC tariff provides the following storage-allocation formula:

> For purposes of reporting storage inventories for state ad valorem taxes, the total inventories of Gas in Market Area Storage Facilities and Field Area Storage Facilities in any particular state … shall be allocated to all Shippers … based on the ratio of total inventories for the state divided by total Storage inventories for all states times the Shipper's total Stored Volume under such Rate Schedules.

Id. at 4a-5a.

The Kansas Property Valuation Division (PVD) uses this FERC-approved tariff to determine each petitioner's stake in each pipeline's Kansas storage facility. Pet. 4a-5a. The pipelines reported to the PVD each petitioner's share of stored gas in Kansas, *id.* at 48a, and petitioners do not challenge this allocation methodology, *id.* at 5a.

This stored gas is the gas that Kansas seeks to tax—not gas that "*may* transiently appear under Kansas soil at some time," Pet. 2—but gas that is *actually stored* in underground storage facilities in Kansas on January 1 of each year when the ad valorem tax is assessed. *Id*. at 46a-47a; *see also* Kan. Stat. Ann. § 79-101. This stored gas is no less petitioners' property than the gas petitioners designate for withdrawal at various times and places.

Because petitioners' property—their share of stored gas in Kansas—is physically present in Kansas when taxed, that stored gas is properly subject to Kansas' generally applicable ad valorem tax. Where petitioners initially delivered the gas to a pipeline, or where they ultimately may receive and sell the gas, is legally irrelevant.

How The Kansas Ad Valorem Tax Works.

All property in Kansas is subject to an ad valorem property tax, unless otherwise exempted. Kan. Stat. Ann. § 79-101. Kansas law exempts from ad valorem taxation "[p]ersonal property which is moving in interstate commerce" through the State, Kan. Stat. Ann. § 79-201f(a), and "merchants' and manufacturers' inventory," *id.* § 79-201m. But it expressly does not exempt from taxation "public utility inventories," which are "subject to taxation pursuant to K.S.A. 79-5a01 et seq., and amendments thereto." *Id.* § 79-201f(a); *see also id.* § 79-201m(b).

In 2009, the PVD determined that petitioners were "public utilities" under Kan. Stat. Ann. § 79-5a01. Pet. 4a. To determine the quantity of stored gas each petitioner owned, the PVD turned to the FERC-approved tariff (discussed above) that specifically addressed the allocation of storage inventories for purposes of state ad valorem taxes. Pet. 4a-5a.

Petitioners deride this allocation formula as "arbitrarily" attributing "fictional ownership" of gas to them. Pet. 6. But this is the allocation formula petitioners agreed to use to determine ownership of stored gas for purposes of state ad valorem taxes. Pet. 5a. And just because no one can say for sure whether the particular molecules of gas in storage in Kansas are the molecules that petitioners tendered to the pipeline initially, does not mean that petitioners' share of the gas stored in Kansas is "fictional" and is thus exempt from taxation.

Petitioners' ownership of a portion of the gas stored in Kansas is no more ephemeral than petitioners' ownership of the gas they withdraw from the pipelines at various times and places. Petitioners retain title to the gas they deposit in the pipelines, and the FERC-approved allocation formula is how petitioners agreed to allocate their share of that commingled gas for purposes of paying state ad valorem taxes. As "[c]ustomers that contract with a pipeline for delivery of natural gas," petitioners are "bound by" the FERC-approved tariff. Pet. 47a. Moreover, petitioners "d[id] not challenge this allocation methodology" in the Kansas Supreme Court. *Id*. at 5a.

Petitioners' Unsuccessful Challenges To The Tax.

1. *The Kansas Court of Tax Appeals*. After the PVD assessed the ad valorem taxes, petitioners appealed that decision to the Kansas Court of Tax Appeals (KCOTA). Petitioners argued that the gas at issue was exempt from taxation under various state laws and the Kansas Constitution, Pet. 5a, 45a, and that the tax violated the Dormant Commerce, Due Process, and Import-Export Clauses of the U.S. Constitution, *id.* at 5a. Petitioners also contested PVD's use of the FERC-approved allocation formula to determine their share of the gas stored in Kansas. *Id.*

After a hearing, the KCOTA affirmed the tax assessments, denied petitioners' requests for exemption, *id.* at 56a, and rejected petitioners' attack on the allocation formula because they "did not present any evidence that th[e] allocation was … improper" and failed to offer an alternative formula, *id.* at 64a. *See also id.* at 10a. The KCOTA presumed, as it must, that the Kansas tax statutes were "constitutional as drafted." *Id.* at 56a.

2. *The Kansas Supreme Court*. Petitioners appealed the KCOTA decision to the Kansas Supreme Court. In the Kansas Supreme Court, petitioners argued that they were exempt from taxation under Kansas law and the Kansas Constitution, and that the ad valorem tax violated the Dormant Commerce and Due Process Clauses of the U.S. Constitution. Pet. 10a-11a. The Kansas Supreme Court held that petitioners are not exempt from taxation under Kansas law, and rejected their arguments that the ad valorem tax violated the federal Constitution. *Id*. at 21a, 23a.

With respect to the Dormant Commerce Clause claim—which is the *only* claim the petitioners press in their petition for a writ of certiorari in this Court—the Kansas Supreme Court addressed two and only two legal questions. *First*, that court described the petitioners' "threshold argument" as relying on the "Supreme Court's *Quill* decision" to argue that "the four-part *Complete Auto* analysis does not govern their Commerce Clause claim because the tax here violates a bright-line rule prohibiting states from assessing taxes if the assessees' only connection with the state is through a common carrier." Pet. 14a. The court read *Quill* to establish the rule that a "state may not impose a use tax on an out-of-state vendor whose only connection with the state is through a common carrier." *Id*. at 15a.

The Kansas court acknowledged that there "is a split of authority in our sister states on whether the Court's holding in *Quill* is limited to sales and use taxes." Pet. 15a (citing a New Jersey Supreme Court case which in turn cites cases from the North Carolina Court of Appeals and the Tennessee Court of Appeals). The Kansas Supreme Court agreed with the New Jersey Supreme Court that "*Quill* is best restricted to sales and use taxes," *id*. at 16a, becoming only the second state supreme court to decide that question. The Kansas Supreme Court thus held that the *Quill* rule is inapplicable to the Kansas ad valorem tax.

Second, the Kansas court observed that the "taxpayers' second Commerce Clause argument relates to the *Complete Auto* test …." Pet. 16a. "Taxpayers argue the tax violates the first and fourth prongs of the *Complete Auto* test, *i.e*., the tax is neither fairly apportioned, nor fairly related to services provided by the state." *Id*. After noting that the two prongs are related and both require a "substantial nexus" to the taxing jurisdiction, *id*., the Kansas court acknowledged that the Oklahoma Supreme Court and the Texas Court of Appeals have disagreed on the application of *Complete Auto* to an ad valorem tax on natural gas stored in an interstate pipeline system. *Id*. at 17a. The Kansas Supreme Court "agree[d] with the Oklahoma Supreme Court" and held that "these taxes do not violate the Commerce Clause." *Id*.

Ultimately, the Kansas court concluded that "[w]e agree with the Oklahoma Supreme Court that the most important factor in determining whether a substantial nexus exists to tax the taxpayers' gas is that this is a personal property tax on stored natural gas that was located in Kansas on the assessment date." Pet. 21a. Thus, the court rejected "the taxpayers' arguments that ad valorem taxation of their stored natural gas fails to satisfy the first and fourth prongs of the *Complete Auto* test." *Id*. Instead, "[t]here is axiomatically a substantial nexus between Kansas and the gas stored in this state," and there was no differential tax rate between the natural gas at issue here and other personal property subject to ad valorem taxation in Kansas. *Id*.

Nowhere in its opinion does the Kansas Supreme Court address or decide the "goods-in-transit" argument petitioners now make in this Court. Nor did petitioners' briefs filed in the Kansas Supreme Court ever invoke that phrase or even cite the primary cases upon which they rely in this Court.

REASONS FOR DENYING THE WRIT

I. PETITIONERS DID NOT MAKE A "GOODS-IN-TRANSIT" ARGUMENT BELOW, NOR DID THE KANSAS SUPREME COURT DECIDE THAT QUESTION, NOR IS THERE A SPLIT OF AUTHORITY ON THE QUESTION, NOR IS THERE ANY MERIT TO THE ARGUMENT IN THIS CASE.

A. The Kansas Supreme Court Did Not Address Or Decide The "Goods-In-Transit" Argument Petitioners Press In This Court, Nor Did Petitioners Ever Invoke That Phrase In Their Briefs Below Or Even Cite Most Of The Cases On Which They Now Rely.

There is no mention of a "goods-in-transit" doctrine in the Kansas Supreme Court's opinion. No mention, no discussion, no decision. That is not surprising given that petitioners below never used that phrase, never clearly articulated any such argument, and never even cited most of the cases upon which they now rely; cases such as *Coe v. Errol*, 116 U.S. 517 (1886), *Kelley v. Rhoads*, 188 U.S. 1 (1903), *Champlain Realty Co. v. Town of Brattleboro*, 260 U.S. 366 (1922), *Carson Petroleum Co. v. Vial*, 279 U.S. 95 (1929), and *D.H. Holmes Co. v. McNamara*, 486 U.S. 24 (1988). *See* Pet. 21-27.

In fact, the closest petitioners came to even implying such an argument in the Kansas Supreme Court is their opening brief at pages 28-31 where they relied on a Tenth Circuit case and a Kansas Supreme Court case to argue that their "gas is exempt from taxation … because it is moving in interstate commerce." Opening Applt. Br. at 28. Even then, however, the only two decisions of this Court that petitioners cited in support of their claim were Import-Export Clause cases, *id*. at 30-31, not Dormant Commerce Clause cases, and petitioners further muddled any potential constitutional argument by urging that the Kansas Supreme Court "should find that the gas is exempt under the provisions of K.S.A. 79-201f," *id*. at 31, arguing that the statute (*i.e*., state law) excludes such gas from ad valorem taxation.

B. Any "Goods-In-Transit" Claim Does Not Present A Split Of Authority And Fails On The Merits.

Petitioners notably fail even to attempt to demonstrate a split of authority between state courts of last resort or federal Circuits on whether a "goods-in-transit" doctrine applies to natural gas that has moved in interstate pipeline systems so that such gas may not be taxed by states where the gas is stored. *See* Pet. 27 ("C. The Kansas Supreme Court Departed From This Court's Directly Applicable Precedents"); *id*. at 30 ("D. Lower Courts Are Confused About The Proper Analytical Framework").

Nor could they prevail on such a claim on the merits even if such a claim (1) was properly before the Court and (2) involved a split of authority justifying a grant of certiorari. Although the Court long ago suggested that there could be *no* state or local taxes imposed on interstate commerce, *see Leloup v. Port of Mobile*, 127 U.S. 640, 648 (1888) ("no state has the right to lay a tax on interstate commerce in any form"), those days are ancient history. Instead, for over 100 years the Court has recognized that even goods temporarily located in a state may be subject to taxation by that state, at least in many circumstances.

For example, in *Bacon v. Illinois*, 227 U.S. 504 (1913), the Court upheld a tax on grain located in an elevator in Chicago even though the owner had no intention of keeping the grain in Chicago other than "for the sole purposes of inspecting, weighing, grading, mixing, etc." before shipping the grain out of Illinois. 227 U.S. at 515. *Id*. ("No part of the grain was sold or consumed in Illinois.") The Court upheld the Illinois tax, observing that the grain "was not being actually transported" when taxed. *Id*. at 516.

Similarly, *Susquehanna Coal Co. v. Mayor of South Amboy*, 228 U.S. 665 (1913), involved coal which was shipped by rail to a storage facility where it was held until shipped outside the state to the ultimate consumers. The Court held that the stored coal could be taxed, even though its presence in the state was in some sense "temporary," not least because "without such accumulations the orders might strike a period when there were no cars and no coal, and then customers would suffer." 228 U.S. at 669. As the Court emphasized, "[i]t is clear, we repeat, that such trade could only be accommodated through the storage of coal somewhere …." *Id*. "The coal, therefore, was not in actual movement through the state; it was at rest in the state, and was to be handled and distributed from there." *Id*.

Most analogous to this case is *Independent Warehouses, Inc. v. Scheele*, 331 U.S. 70 (1947), in which the Court again upheld a tax on coal stored in the taxing state even though "at the time the tax is laid it cannot be determined what the ultimate destination or use of the property may be." 331 U.S. at 81. "Indeed, at the actual time of storage, even the owner may not know where the coal will go next, for the very purpose of the storage is in part to meet seasonal demand." *Id*.

Scheele emphasized that "the duration of the cessation of transit is indefinite," and that "invariably the goods are fungibles, a fact pointing up the fictional basis of the in transit privilege." 331 U.S. at 82. Describing the coal at issue, the Court observed that the "goods which are sent initially into the interstate commerce stream are not the identical goods which finally arrive at the place of consumption." *Id*. Taken together, the Court's conclusion was that, "[i]n view of all these considerations, the case falls more appropriately in the category allowing the state's taxing power to apply, than in one denying its applicability." *Id*.

One could simply insert "natural gas" for "coal" in the *Scheele* opinion and the outcome in this case would be utterly clear. Further, *Scheele* makes it apparent that Kansas has the power to impose the ad valorem tax here notwithstanding the so-called "goods-in-transit" doctrine. Kansas *only* taxes natural gas *stored* in underground formations in the state; it does *not* tax natural gas that is never stored and simply moves through pipelines that cross Kansas. Thus, the only natural gas Kansas taxes here is the gas which is stored in Kansas for the beneficial business purposes of the taxpayers—to accumulate gas in storage when supply is plentiful and the price is low in order to meet higher demands by customers during other seasons of the year, among other benefits.

Like *Scheele*, this case does not involve state taxation of a good that never stops moving as it is transported across the state, or one that stops only briefly and "incidentally," or as dictated by "necessities or convenience." 331 U.S. at 84. Nor does the fact that much of the gas stored in Kansas ultimately will move across Kansas' borders to other states make any difference, as *Scheele* again makes clear: "the fact that this movement crosses a state line makes it of course an interstate movement. But this does not make it part of a continuous journey beginning at the mine and ending in the second state of destination." *Id*.[1]

[1] *Scheele* necessarily rejects the argument of petitioners and their *amici* that, because FERC (for reasons wholly unrelated to state taxation) defines interstate "transportation" of natural gas to include "storage," *see Schneidewind v. ANR Pipeline Co*., 485 U.S. 293, 295 n.1 (1988), any storage of natural gas is automatically a good in transit for Commerce Clause purposes. The argument is a non-sequitur, as the Oklahoma Supreme Court easily concluded, *In re Assessment of Pers. Prop. Taxes Against Missouri Gas Energy*, 234 P.3d 938, 955-957 (Okla. 2008), and the United States agreed when it recommended denial of certiorari in that case. *See* Br. for U.S. in No. 08-1458, at 16 ("the FERC regulation does not bear on the analytically distinct question whether stored natural gas has a sufficient nexus to the State in which storage occurs to permit state taxation under the *Complete Auto* test").

II. THE TWO QUESTIONS THE KANSAS SUPREME COURT ACTUALLY DECIDED DO NOT INVOLVE SPLITS OF AUTHORITY BETWEEN STATE COURTS OF LAST RESORT OR FEDERAL CIRCUITS, NOR DID THE KANSAS SUPREME COURT DECIDE THOSE QUESTIONS INCONSISTENTLY WITH THIS COURT'S DECISIONS.

A. Petitioners Fail To Identify The Actual Legal Questions Presented In This Case.

Petitioners' Question Presented is phrased as a general "dormant Commerce Clause" challenge based on the asserted facts that their gas "is being transported through interstate commerce" and only "temporarily stored" in Kansas by a "common carrier. Pet. i. Further, petitioners assert that they have "no control over where the gas is stored and no other connection with Kansas." *Id*. Petitioners' question is potentially misleading, both on the facts and the legal issues.

With regard to the facts, there is no question that natural gas is fungible. Once gas is commingled in a pipeline, it may be impossible for anyone to know the source of any particular molecule of gas, or to readily identify any particular molecule at any point in the pipeline system. But there also is no question that significant quantities of natural gas are stored in Kansas for significant periods of time, and such storage occurs for the financial benefit of the owners of the gas such as petitioners.

Petitioners' "facts" as asserted in the Question Presented thus make several leaps to incorrect or debatable conclusions petitioners find helpful to their argument (*e.g.*, the gas is "being transported" when taxed by Kansas, the gas is only "temporarily stored" in Kansas, and petitioners have "no control over where the gas is stored," even though they certainly know, anticipate, and desire that it be stored in various places along the pipeline system because such storage is essential to the success of their businesses).

Furthermore, as a legal matter, the Kansas Supreme Court could not have been clearer that it decided only two legal questions. The first was whether the "physical presence" rule of *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), applies to ad valorem taxes like the Kansas tax at issue here. The Kansas court held that the *Quill* rule does not apply here, and so proceeded to the second question. The second question was whether the Kansas tax satisfies the *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), test. Those are the only legal questions the Kansas Supreme Court decided in resolving petitioners' Dormant Commerce Clause challenge; they are thus the only two legal issues truly and properly presented for this Court's consideration in the petition for a writ of certiorari.

B. The Question Whether The *Quill* Physical Presence Rule Applies To Ad Valorem Taxes Implicates No Split Of Authority Between State Courts Of Last Resort Or Federal Circuits And Does Not Otherwise Merit A Grant Of Certiorari.

Supreme Court Rule 10.1(b) makes clear that a grant of the writ of certiorari to review a state supreme court is warranted only when such a court "has decided an important federal question in a way that conflicts with the decision of another state court of last resort or of a United States court of appeals." Petitioners completely fail to satisfy that standard; indeed, they don't even claim to do so, instead arguing that, at most, there is "confusion" in the "lower courts" about how to decide cases such as this.

Petitioners cite four state cases at page 29 of their petition for the proposition that the Kansas Supreme Court's "unduly restrictive reading of *National Bellas Hess*[, *Inc., v. Dept. of Revenue of Ill.*, 386 U.S. 753 (1967)] and *Quill* has itself divided state courts." Notably, however, they cite only one state supreme court decision (*Lanco, Inc. v. Director, Div. of Taxation*, 908 A.2d 176, 177 (N.J. 2006) (per curiam)), the very case with which the Kansas Supreme Court explicitly *agreed*. *See* Pet. 16a ("We agree with the *Lanco* court.") Thus, the only two state supreme courts to have considered the issue are in complete agreement.

Furthermore, none of the cases cited to show the "split" involved state ad valorem taxes, so they are in that sense all distinguishable from this case. *See Lanco* (corporation business tax); *A&F Trademark, Inc. v. Tolson*, 605 S.E.2d 187 (N.C. Ct. App. 2004) (corporate franchise and income taxes); *Rylander v. Bandag Licensing Corp.*, 18 S.W.3d 296 (Tex. Ct. App. 2000) (franchise tax); *J.C. Penney Nat'l Bank v. Johnson*, 19 S.W.3d 831 (Tenn. Ct. App. 2000) (franchise and excise taxes). That distinction is potentially fundamental because, as the Kansas Supreme Court observed, in the specific context of an ad valorem tax "[t]here is axiomatically a substantial nexus between Kansas and the gas stored in this state." Pet. 21a.

For all of these reasons, petitioners have failed to identify a split of authority regarding the *Quill* rule that merits a grant of certiorari.

C. The Question Whether The Kansas Ad Valorem Tax Satisfies The Four-Part *Complete Auto* Test Implicates No Split Of Authority Between State Courts of Last Resort Or Federal Circuits And Does Not Otherwise Merit A Grant of Certiorari.

As is true of the *Quill* issue, petitioners have failed to identify any relevant split of authority regarding the application of the *Compete Auto* test to the facts presented here. There are only two other decided cases besides the Kansas case, and the Kansas Supreme Court explicitly agreed with the only other state supreme court decision in this regard. In any event, the application of *Complete Auto* here is a factbound question that does not implicate any novel or unsettled legal issues.

Apart from this case, the only two cases petitioners argue contribute to lower court "confusion" are *In re Assessment of Personal Property Taxes Against Missouri Gas Energy*, 234 P.3d 938 (Okla. 2008), *cert. denied*, 559 U.S. 970 (2010), and *Peoples Gas, Light & Coke Co. v. Harrison Central Appraisal District*, 270 S.W.3d 208 (Tex. Ct. App. 2008), *review denied*, 2010 Tex. LEXIS 227 (Tex. 2010), *cert. denied*, 131 S. Ct. 2097 (2011). Under this Court's rules, only the decisions of state courts of last resort and federal Circuits matter for purposes of determining a split, and there is no such division of authority here, with the Kansas and Oklahoma Supreme Courts in agreement on the application of *Complete Auto* in this context. *See* Pet. 17a ("we agree with the Oklahoma Supreme Court and hold that these taxes do not violate the Commerce Clause").

The only contrary decision is an intermediate appellate court decision from Texas, a case in which both the Texas Supreme Court and this Court denied further review. Kansas certainly recognizes that the Texas decision is inconsistent with the Oklahoma and Kansas decisions, but it is not the ultimate decision of a state in the sense this Court contemplates when considering a grant of certiorari. Indeed, the Texas Supreme Court never spoke on the merits of the Texas case or taxation scheme.[2]

Furthermore, this Court declined the opportunity to review either the Oklahoma or Texas cases, even though the Court was well aware that the two cases had reached contrary conclusions. The Court denied certiorari review first in the Oklahoma case following a recommendation by the Solicitor General that review be denied because, among other things, "the Oklahoma Supreme Court applied the correct legal standard" and "reached the correct result." Br. for U.S. in No. 08-1458, at 6. The Court later denied review in the Texas case, which presented the same conflict-of-authority arguments that petitioners raise here, *see* Pet. in No. 10-896, at 4, without even requesting the Solicitor General's views. Now, just as in 2011, the conflict

[2] A leading state taxation treatise criticizes the Texas decision, explaining that the "court's conclusion that 'the significant volume of natural gas … in the storage facility' was not sufficient to satisfy Complete Auto's first and fourth prongs is highly questionable, if not plain error. The physical presence of a 'significant volume' of the owner's property appears to be more than sufficient to constitute 'substantial nexus.'" Walter Hellerstein, 1 *State Taxation* (3d ed. 2013) ¶ 4.13[3][a], at 11.

between the Texas Court of Appeals and the Oklahoma Supreme Court does not warrant review. Indeed, that the Kansas Supreme Court agreed with the Oklahoma Supreme Court counsels *in favor of denying review*, not granting it.

Finally, the Kansas Supreme Court's decision is correct on the merits. Petitioners' legal position suggests that no state could ever tax natural gas that has moved in interstate pipelines unless and until such gas is actually consumed in the state. Such an extreme result cannot stand in the face of the Court's many cases allowing states to impose a variety of taxes on items that move in interstate commerce but which are stored in states for various times and reasons before moving again across state lines. As discussed above, the Court has a long line of cases permitting state taxes to be imposed on goods stored in a state, even though the goods later would be shipped to another state for ultimate use or consumption.[3]

---

[3] Indeed, the Solicitor General informed the Court that the Oklahoma Supreme Court's decision upholding the Oklahoma tax on natural gas stored in Oklahoma "reflects a sound application of the first ('substantial nexus') prong of the *Complete Auto* test, as well as comporting with the 'continuity of transit' cases focusing on the purpose of the interruption." Br. for U.S. in No. 08-1458, at 14. A leading treatise also approved of the "Oklahoma court explicitly refrain[ing] from even addressing the 'in transit' question, because it believed (correctly, in our view, on the basis of *Holmes* and its progeny) that this question was irrelevant for purposes of Commerce Clause analysis." Hellerstein, *supra* note 2, *State Taxation* ¶ 4.13[3][a], at 12. Similarly, the treatise concludes that the Kansas Supreme Court, in this case, "after thoughtfully analyzing the issues in light of the precedents, concluded (properly, in our view) that the levies do not violate the Commerce Clause." *Id*. at 13.

Petitioners want all of the benefits of the pipelines' actual storage of petitioners' gas, benefits that among other things make it possible for petitioners' businesses to succeed, but they seek to avoid any tax liability for the benefits that Kansas provides regarding such storage. The Dormant Commerce Clause does not compel that result; indeed the Court's cases long have rejected that very outcome, and allowed the imposition of a variety of state taxes in circumstances similar to those presented here.

At bottom, petitioners' constitutional argument would lead to the legal conclusion that no state can tax natural gas stored in that state based on the presence of such personal property in the state's jurisdiction, no matter how long the storage might occur, as long as the gas may at some future time be transported to another state. Essentially, petitioners are asking the Court to impose a legal regime that permits taxation—at most—of natural gas only where it is ultimately consumed (and perhaps a severance tax where it is first extracted from the ground).

CONCLUSION

The Kansas Supreme Court did not even mention—much less decide—one of the primary arguments petitioners' now raise, nor did petitioners clearly present that argument to the court below. Furthermore, petitioners fail to clearly identify the actual legal questions presented here. In any event, petitioners fail to demonstrate a split of authority between state courts of last resort or federal Circuits on any issue in this case. The petition does not merit an exercise of this Court's certiorari review, and should be denied.

Respectfully submitted.

DEREK SCHMIDT
Attorney General of Kansas
STEPHEN R. McALLISTER
Solicitor General of Kansas
(*Counsel of Record*)
JEFFREY A. CHANAY
Deputy Attorney General
BRYAN C. CLARK
Assistant Solicitor General
120 S.W. 10th Avenue, 2nd Floor
Topeka, KS 66612
Telephone: (785) 296-2215
steve.mcallister@trqlaw.com

WILLIAM E. WATERS
Special Assistant Attorney General
Division of Property Valuation
Kansas Department of Revenue
Docking State Office Building, 4th Floor
915 S.W. Harrison Street
Topeka, KS 66612
Telephone: (785) 296-4035

Counsel for Respondent
the State of Kansas

May 29, 2014