

BEFORE THE STATE TAX APPEAL BOARD
OF THE STATE OF MONTANA

THE WILLIAMS COMPANIES, INC.)	
and SUBSIDIARIES,)	DOCKET NO.: CT-1996-1
)	
Appellant,)	
)	
-vs-)	
)	
THE DEPARTMENT OF REVENUE)	FINDINGS OF FACT,
OF THE STATE OF MONTANA,)	CONCLUSIONS OF LAW,
)	ORDER and OPPORTUNITY
Respondent.)	<u>FOR JUDICIAL REVIEW</u>

The above-entitled appeal was heard July 27, 1998 in the City of Helena, Montana, in accordance with an order of the State Tax Appeal Board of the State of Montana (hereinafter referred to as the **AB**oard®). The notice of the hearing was given as required by law. The Appellant was represented by attorneys Terry B. Cosgrove, Maryann B. Gall, and Rose Mary Ham. The Respondent was represented by attorneys Brendan Beatty and David Woodgerd.

At this time and place, testimony was presented and exhibits were received. The hearing was continued and reconvened on December 11, 1998 in the City of Helena, Montana for the purpose of hearing a Respondent's surrebuttal witness.

The Board having fully considered the testimony, exhibits, and all things and matters presented to it for its

consideration by all parties, and being well and fully advised finds and concludes as follows:

STATEMENT OF THE ISSUE

The issue before this Board is whether Northwest Alaskan Pipeline Company, a wholly owned subsidiary of THE WILLIAMS COMPANIES, INC., has taxable nexus with the State of Montana, providing a basis for an assessment of additional taxes and interest as determined by the Montana Department of Revenue.

FINDINGS OF FACT

1. Due, proper, and sufficient notice was given of this matter, the hearing, and of the time and place of the hearing. All parties were afforded opportunity to present evidence, oral and documentary.

2. This Board has jurisdiction to hear and decide this matter.

3. The Department of Revenue (hereinafter referred to as **ADOR@**) conducted an audit of The Williams Companies, Inc. and Subsidiaries (hereinafter referred to as **AWilliams@**) for the tax years ending December 31, 1987 through December 31, 1993.

As a result of this audit the DOR issued a Notice of Proposed Assessment by letter of July 25, 1995.

4. Following an informal conference and review with the Appellant, the DOR through Mr. Lynn Chenowith, Bureau Chief

of the Corporation Tax Bureau, upheld assessments as set forth in a letter of November 17, 1995 that stated, in pertinent part:

It is the division's determination that Northwest Alaskan Pipeline Company has sufficient activities in the state of Montana to create nexus and that natural gas destination sales made into the state of Montana have been correctly included in the Montana Sales Numerator for all years of the audit.

5. Northwest Alaskan Pipeline Company (hereinafter referred to as ANWA@), is a wholly owned subsidiary of Williams, a Delaware corporation.

6. Northwest Border Pipeline Company (hereinafter referred to as ANWB@) is also a wholly owned subsidiary of Williams. NWB owns 12.25% of the Northern Border Natural Gas Pipeline which enters Montana from Canada near Port of Morgan, Montana. (Jt Ex 44)

7. The Appellant filed an objection with the DOR Director; and the Appellant filed an appeal with this Board.

8. Pursuant to ' 15-1-211(6)(b) Montana Code Annotated, the Director of the Department of Revenue elected not to review the department's decision in this matter.

9. In addition to the objection identified in Finding 2, the Appellant's Petition of January 11, 1996 contained an additional five objections to the DOR's final determination as set forth in the DOR's letter of November 17,

1995; the Appellant's Second (and final) Amended Petition of March 9, 1998 set out a single issue as identified in Finding 2 and set out in the Statement of the Issue of this decision.

10. NWA was formed to hold the partnership interests of the Alaskan Northwest Natural Gas Transportation Company (hereinafter referred to as ANNGTC), which was the partnership company formed to build the Alaska portion of the Alaskan Natural Gas Transportation System (hereinafter referred to as ANGTS).

11. During the Audit Period, NWA's primary business was acting as managing partner of the ANNGTC. (Jt Ex 37) NWA also held an import permit, issued by the Federal Energy Regulatory Commission (hereinafter referred to as FERC), which permitted NWA to import 800 million cubic feet of Canadian natural gas into the United States each day. (Jt Ex 10)

12. The federal governments of Canada and the United States required parties selling gas from Canada to hold export permits issued by Canada's National Energy Board and import permits issued by the United States FERC. (Tr I pg 33)

13. NWA secured the import permit from FERC which permitted it to purchase 800 million cubic feet of Canadian gas each day from Pan-Alberta Gas at the International Boundary, import the gas into the United States, and resell the gas to several U.S. purchasers. (Tr II pg 42, Jt Ex 10)

14. NWA entered into Gas Purchase and Gas Sales agreements with Pan-Alberta and the U.S. purchasers. The contracts specifically provided that when NWA purchased the gas, it held title to, and was deemed to be in control and possession of, the gas. The contracts provided that NWA would deliver the gas to the U.S. purchasers in the United States. (Jt Ex 11, 12, Ex R-17, Tr III pg 9)

15. NWA reported its Eastern Leg natural gas sales as Montana sales on its Montana Corporation License Tax Returns for the years 1987 to 1991. (Jt Ex 15, 16, 17)

16. NWA has no employees. (Tr II pg 210) NWA does not own any gas pipeline, compressor stations, or other pipeline parts. (Tr II pg 199)

17. NWA owned tangible personal property in Montana on a continuous basis at all times during the audit period. (Tr I pg 154, II pg 218, III pg 187, 188, IV pg 196) NWA sold and delivered tangible personal property to its purchasers in Montana during the audit period. (Tr IV pg 196, 197)

18. Any proposed findings not adopted by this Board are hereby rejected by this Board.

APPELLANT-S CONTENTIONS

19. Appellant-s counsel summarized the two primary bases upon which the DOR assessment was appealed: 1) NWA does not have nexus with the State of Montana; and 2) NWA **A**...has

always operated on a no-profit no-gain basis@ operating as an accommodation as A...part of a large national and international energy project@. (Tr I pgs 7-8)

20. Cuba Wadlington, Jr., former vice president of NWA, testified that NWA was formed to hold the partnership interests of the 15 partners of ANNGTC, the partnership company formed to build the Alaska portion of the ANGTS. He stated that Pan-Alberta Gas Limited owned the export permit needed to sell Canadian gas to NWA at the international border. (Tr I pgs 14-15)

21. Mr. Wadlington testified the U.S. Congress passed the Alaska Natural Gas Transportation Act (hereinafter referred to as ~~A~~ANGTA@) that provided the means of selection of the transportation system to move gas from Prudhoe Bay, Alaska to the lower 48 states; and there were essentially three proposals (Jt Ex 7). The proposal selected was the Alcan II project: the section from Prudhoe Bay to the Alaskan/Canadian border was owned by a partnership of U.S. companies; and the sections from that border to the U.S. border of the lower 48 states were owned by Canadian interests. An international treaty reflected joint U.S. and Canadian approval of the system, but it was a private enterprise project. (Tr I pg 19-30)

22. Mr. Wadlington stated the section that is

pertinent to this appeal, the Eastern Leg of the ANGTS, started at Caroline Junction and went through Monchy, Saskatchewan and was intended to run all the way to Illinois but actually stopped at Ventura, Iowa (Jt Ex 8) where it could connect with U.S. pipeline systems for further distribution. (The Western Leg started at the British Columbia international border and was to run to southern California.) While environmental approvals and funding were being sought for the Alaskan and northern Canadian sections, it was decided to pre-build a portion of the system in order to move Canadian natural gas on that pre-built portion into the United States to meet energy demands. The pre-built Canadian portion of the pipeline was built by Foothills Pipeline, a subsidiary of NOVA; and Mr. Wadlington testified there was no affiliation between Foothills or NOVA with Williams or NWA. The Canadian portion ends at the Canadian/U.S. international border. The U.S. portion of the pre-built system was Northern Border Pipeline Company and started at the international boundary and terminated in Ventura, Iowa. Mr. Wadlington stated it was anticipated the revenues from the pre-built portion would provide income that would help partners provide equity contributions to the Alaskan partnership when the Alaskan portion of the system was built. (Tr I pg 20-30)

23. Mr. Wadlington stated the Federal Power

Commission, now known as the Federal Energy Regulatory Commission (FERC), had the regulatory authority over the proposed Alaskan natural gas transportation; and on April 5, 1978, NWA filed an application for authorization to import natural gas from Canada and, subsequently, received that import permit. (Jt Ex 9) Mr. Wadlington stated NWA was the entity to apply because buyers of the gas believed NWA was most likely to receive authorization due to its relationship with the Canadian partners in the Alaskan project and with the Canadian government.

Mr. Wadlington testified NWA did not have any use for the natural gas as it didn't have any end-use customers. The market for the gas on the Eastern Leg of the pipeline was through three customers: Northern Natural Gas, United Gas Pipeline, and Panhandle Eastern. Joint Exhibit 10-A was identified by Mr. Wadlington as a series of all the authorizations to allow the gas to be imported at the international boundary between Canada and the United States and sold to U.S. buyers. The Eastern Leg of the pipeline went into service in September, 1982. (Tr I pg 20, 32-35, 37)

24. Mr. Wadlington explained that the portion of the pipeline from Prudhoe Bay to Caroline Junction has not been built because events subsequent to 1978 made the economics of building substantially difficult to justify; it is anticipated

this will be reversed at a future time when economics support resumption of building plans. (Tr I pg 36-37)

25. Mr. Wadlington stated NWA did not build nor was it involved in the building of the Eastern Leg of the pipeline.

He stated NWA does not have an ownership interest in the pre-built system. He explained the original ownership of Northern Border Pipeline Company, the U.S. pipeline that interconnects with the Canadian portion of the system at Monchy, Saskatchewan, was a partnership involving Enron (formerly Northern Natural), Williams, Duke Energy (formerly Panhandle Eastern) and United Gas Pipeline. Northern Plains, a subsidiary of Northern (now a subsidiary of Northern's parent Enron) operates the Northern Border Pipeline, that is, the day-to-day business activities and the natural gas transmission.

Mr. Wadlington stated that, during the audit period, Williams had a 12 percent interest in Northern Border Pipeline. (Tr I pg 38-39, 54)

26. Mr. Wadlington testified that NWA does not take possession of the Canadian natural gas in the state of Montana.

He explained, **A...**the gas is delivered through the Foothills system to the international boundary. Northwest Alaskan buys the gas from Pan-Alberta at the international boundary and instantaneously sells the gas at the international boundary to the three U.S. buyers, that being Panhandle, Northern, and

United.if you could take a snapshot in time....the gas stops in place for a matter-of-second period of time, and several transactions take place while it is stopped in place at the international boundary.a sell by Pan-Alberta, a purchase by Northwest, by NWA, and a re-sell by NWA to United, Panhandle, and Northern.® In another explanation, Mr. Wadlington stated, AWe take title and get rid of title in what I call this dead zone. And the dead zone being the international boundary. Because if we had title inside the United States, that would mean that we had title of the gas while it was on the Northern Border Pipeline. Therefore, we would be responsible for transportation charges on the Northern Border Pipeline....It is sort of in a nano second time frame.® And then that gas moves on down the Northern Border system and as it is moving....it is crossing Montana.®

Mr. Wadlington added, ANWA has never made a profit from the conduit role that it plays with respect to this overall transaction. It was never intended by the parties that NWA make a profit, and it has never made a profit.® Mr. Wadlington added that NWA has never contributed any operating profit to Williams. AIn fact, NWA has, as a practical matter, been a cost to Williams. Even though the administrative cost under the import arrangement was recouped by NWA, but NWA has had to allocate time or personnel to....an entity and an

exercise wherein it doesn't earn a profit.....Not only has it never made any money, I personally view it as having cost Williams over time, because we have used scarce resources in order to administer the deal.@ (Tr I pg 43-44, 55)

27. Mr. Kenneth A. Williams served in several capacities with the Federal Power Commission and, subsequently, FERC during the period 1979 through 1986. Mr. Williams stated, at the time the import application was made by NWA, the FERC was concerned that whatever project it authorized for the pre-built portion of the pipeline, **A**...it would be consistent ultimately with the Alaskan project....that whatever it authorized would not be incompatible, but would actually enhance the development of the Alaskan project.@ He testified the imports from Canada and the pre-build of the Alaskan natural gas transportation facilities were authorized by FERC. Mr. Williams stated NWA was involved due to the fact that FERC was concerned about the Alaskan project and **A**...it wanted to make certain that it didn't do anything or that nothing was done that disjointed this....@ and **A**not being simply a pre-build to get some gas down from Canada....@ Mr. Williams added that if each company intending to market Canadian gas in the U.S. had to secure import authorization, the duplicative effort for those companies and for FERC would have been considerable. **A**And so it made sense to have one party to have the import

authorization and make all the filings with the FERC. (Tr I pg 72, 90-93)

28. Mr. Williams testified the FERC A...regulates companies that transport or sell gas in interstate commerce.

NWA A...was a company that didn't have facilities in the U.S., but made a sale within the international border and that gas was ultimately transported by the purchaser in interstate commerce. And so that was subject to FERC jurisdiction....

Mr. Williams stated that the regulated company, in this case NWA, was required to file with the FERC proposed charges for the gas it was importing. To the cost of the Canadian gas, NWA was permitted to add administrative costs.

It was required to provide to FERC, twice yearly, the details of the development of those costs. Additionally, there was a true-up mechanism whereby the actual costs and estimated costs would be recovered in a future period. He stated A...the only thing they were allowed to recover was their actual cost. As the Canadian pricing changed, the National Energy Board of Canada approved a demand charge that included Pan-Alberta's costs of negotiating contracts with producers, the costs of gathering the gas, and the costs of transporting the gas on the Foothills pipeline. NWA would then add its administrative costs into that demand charge.

Mr. Williams stated that, during the audit period,

the Canadian government permitted individual U.S. shippers to negotiate directly with Pan-Alberta, resulting in different prices. He clarified that a **Ashipper@** is a customer of Pan-Alberta and a shipper on the Northern Border Pipeline system.

He stated there was no provision for earnings by NWA in its re-sell of the imported gas to the U.S. purchasers or shippers.

NWA did not propose to add any type of profit. He stated that, insofar as FERC was concerned, **A...the only type of margin or mark-up for earnings has to be on investment. And since NWA had no investment, there was no basis for any type of earnings.@**

Mr. Williams clarified **Ainvestment@** as **A...investment in facilities. And those facilities can be the pipeline, meters, compressors, any number of things.@** (Tr I pg 96-102)

29. Mr. Kenneth K. Craig is the manager of planning and analysis in the financial group of Pan-Alberta. He stated Pan-Alberta had no role in the initial ANGTS and became involved only when the pre-build became a viable project. During the audit period, Pan-Alberta obtained gas from its pool of producers and NWA was Pan-Alberta's customer for this Canadian natural gas which allowed Pan-Alberta to deal with one customer and NWA **A...performed the import authorization role@.**

Mr. Craig added, **A...it allowed the downstream customers to have a FERC-approved cost that they could recognize and**

pass....through their rates in the United States.@"

Mr. Craig testified that, under the 1978 gas purchase agreement between Pan-Alberta Gas Limited and NWA (Jt Ex 11), NWA as the buyer of gas from Pan-Alberta was a **A**middle man@" or the **A**...term that I use from the commercial background I have is a flipper. What we do, Pan-Alberta exports under national Energy Board approved license, on the international border, to Northwest Alaskan, who in turn flips it simultaneously to the U.S. customers, after utilizing their import authorization.@"

Mr. Craig added that NWA **A**...does not have possession of the gas, because there is nothing they can do with it at that point, where we called it a nano second....where they transfer title from Pan-Alberta gas to the U.S. customers. In order to take possession of the gas, they would have to have something, some place to put it, something to do with it....they do not have transportation....storage, something like that....they do not have possession....they have title to the gas.@" (Tr I pg 121, 123-130)

30. Mr. Craig testified that, in the period 1989 through 1993, Pan-Alberta undertook a series of negotiations with all three of their major U. S. customers. The result was that all three ceased to buy natural gas from Pan-Alberta, as deregulation of the natural gas industry in the U.S. made it no longer necessary to sell gas to pipeline companies for

distribution companies and marketers were buying the gas directly. The contracts were assumed by the wholly-owned subsidiary of Pan-Alberta in the United States: Pan-Alberta Gas U.S. Inc. (hereinafter referred to as APAG-US@). Mr. Craig stated that PAG-US had, at any given time, A...between 40 and 75 customers on the East Leg.@ (Tr I pg 131-134)

31. Mr. Craig stated that, during the 1987 through 1989 period, when the customers were United, Panhandle, and Northern Natural, the customers would make a nomination for the amount of gas supply requested. He explained, AMy understanding of the word nomination means the request by somebody for an amount of natural gas.@ He stated, AThe buyers would make their requests known to Northern Border Pipeline....the pipeline that would have to transport their supplies. At the same time, they would either fax or phone the order to Pan-Alberta Gas....@ The pipeline would also contact Pan-Alberta to ensure the quantity of gas nominated was agreed upon. He added, ASo, in other words, Northern Border would aggregate the amount of gas required by all Pan-Alberta customers and request that amount of gas from Foothills Pipelines....@ which would A...then go to NOVA to request that amount of gas from NOVA....@ ensuring Pan-Alberta sufficient quantities of gas to meet the nominations.

Mr. Craig stated that the nomination process did not

change when Pan-Alberta took over the contracts from the original three customers. He added that NWA **A...**never was and still is not involved in the nomination process....@ He explained, that Pan-Alberta Gas prepares statements related to their customers= nominations which it sends to NWA, outlining their sales revenue and, at the same time, Pan-Alberta is invoicing NWA for the gas sold. On the statement are the costs that are required to move the gas from the Canadian border where NWA sells the gas to the downstream customers and details those costs so NWA knows what its net costs would be at the Canadian border. To that amount NWA adds its administrative costs. Mr. Craig stated there was never a billing function in Montana; the invoices and statements are sent to NWA's Tulsa office. NWA invoices PAG-US; PAG-US pays NWA which, in turn, deducts its costs and electronically transfers the remaining funds to Pan-Alberta Gas in Canada. (Tr I pg 134-138)

32. Mr. Craig testified that Pan-Alberta Gas. under its contract that is Joint Exhibit 11, delivers its gas on the international border between Canada and the United States. In response to a question of who owns the gas after the sale that occurs in Canada, he stated: **A...**this is the conundrum you get into in the definition of the international boundary....@ and NWA **A...**is just one piece of this quadruple change that occurs at the international border. So I believe that

Northwest Alaskan takes possession of that gas after it is exported, under license from Canada....it has been exported from Canada. It has not yet been imported into the United States. So we are in this dead zone that Mr. Wadlington brought up.@"

He further explained, "Pan-Alberta Gas does not, cannot own that gas in the United States. So we export it, then we sell it, then it is imported, and then it is sold by Northwest Alaskan. So there is no clear definition that says....Pan-Alberta has sold that gas in Canada or the United States. The contractual language says the sale is made on the international boundary. When asked for further clarification as to where the sales transaction occurs, Mr. Craig responded, "The gas is sold on the international border, after export from Canada and before import to the United States." Mr. Craig agreed when asked if he believed that the "international border" was not in either Canada or the United States. (Tr I pg 144-145,148-149)

33. Mr. Craig testified that, during the audit years, the U.S. customers took title to the gas in the United States and the sales occurred in Montana; however, NWA did not deliver the natural gas into Montana. He stated, "The term 'deliver,' in my mind, connotes (sic) the movement of natural gas from a point to another point, however small that may be.

In order to do that, Northwest Alaska would have to have a transportation agreement with a pipeline or another medium to move that natural gas in order to deliver it. Mr. Craig further explained that the goods are not moved, but rather only the title to the goods are transferred. The gas is delivered between two pipelines, one of which has a transportation contract with Pan-Alberta on the Canadian side; and the other one has transportation agreements with the three downstream customers. He stated that, without being moved, the gas is imported on that thin line of the international border on the United States side. (Tr I pg 151-153,155-156)

34. Harry N. Hobbs, vice-president of transportation and public affairs, and secretary of Foothills Pipeline, Ltd. testified about the transportation of Canadian natural gas on that portion of the pipeline system. He stated that Foothills delivers approximately one-third of all natural gas exports to the United States.

Foothills connects with Northern Border Pipeline Company at the international border. He described the location of the gas metering station 20 meters north of the international boundary and stated that NWA has no facilities on this portion of the pipeline. Foothills does not consider NWA to be a shipper on this pipeline, and NWA is not billed by Foothills for transportation of any natural gas on its system.

He stated that customers are billed for transportation of natural gas from the point of receipt to the delivery point.

The final point of delivery on the Foothills system is the international boundary between Canada and the United States. (Tr I pgs 166-184)

Mr. Hobbs testified that NWA was not an owner of natural gas on the Eastern Leg of the Foothills system and that NWA never had an inventory of natural gas stored on Foothills.

Mr. Hobbs stated that he is aware NWA imports natural gas under its authorizations and re-sells that gas to its repurchasers.

35. Mr. Raymond D. Neppl, Northern Plains Natural Gas Company vice-president of regulatory affairs, testified for the appellant. Although formally employed by Northern Plains, his work is dedicated to the Northern Border Pipeline Company, the owner and operator of the pipeline system from the Montana-Saskatchewan border to its points in Iowa.

He testified concerning the international border and the significance of the change in jurisdiction between the National Energy Board in Canada and the FERC in the U.S. He stated that Northern Border has never considered NWA as a shipper on the Northern Border system nor has NWA had storage of any inventory on that system.

He responded to a question concerning the NWA sales

of natural gas, **A**it would be my understanding, I believe that the sales authority would be a U.S. jurisdiction. (Tr I pg 239)

36. Mr. Scott K. Coburn is director of throughput management for Northern Border, although he is an employee of Northern Plains Natural Gas Company. Mr. Coburn testified as to **A**in-line title transfers of natural gas. He explained that, when receipt and delivery occur at the same point one can have **A**zero mileage under that kind of a scenario. (Tr II pg 22) He stated that Northern Border has never charged NWA for transportation of natural gas because NWA is not a **A**shipper on the pipeline, and NWA has no contract to do so on Northern Border's system. He testified that NWA plays no role in the **A**nomination process for natural gas quantities being transported on the pipeline system.

Mr. Coburn referred to the commonality of title transfers of natural gas. He stated that **A**...we've seen title transfers communicated to us that maybe are twelve or thirteen parties long.... (Tr II pg 32)

Mr. Coburn described the relationship of the Port of Morgan to the international boundary as, **A**I would say that international boundary, Port of Morgan, just butts up right against each other. If you want to say that Port of Morgan is in Montana, yes, because I think you have to say that because that's a jurisdictional point on our system. (Tr II pg 47)

Mr. Coburn explained how the gas measurement, nomination process and billing of shippers eventually includes NWA. Pan-Alberta Gas, for part of the period, Northern Border, Pan-Alberta -- or Panhandle Eastern, and United for part of the period. Then in turn those customers have to pay -- they're required to pay Northwest Alaskan. So our documentation that we produce for billing our customers turns -- produces the information you're searching to find. How does Northwest Alaskan know how it's -- It's communicated from our shippers to Northwest Alaskan, which in turn Northwest Alaskan communicates back to the Canadian party. (Tr II pg 75)

37. Mr. Glenn Shearer was employed by United Gas Pipeline Company during the audit period at issue in this appeal. United Gas was a purchaser of the imported natural gas. He testified to very little contact with NWA but to at least monthly meetings with Pan-Alberta Gas. United Gas paid NWA for the gas received due to import/export license requirements even though the prices were negotiated with Pan-Alberta.

Mr. Shearer considered that United took possession of the gas at the international border at Mile Post 0.00 and that point is in the United States, yes. (Tr II pg 92)

RESPONDENT-S CONTENTIONS

38. Exhibit J-29 is a FERC form number two filed by NWA for the year ended December 31, 1987. DOR witness Mr. George Donkin referred to that exhibit as one reviewed by him in making the determination that NWA sells natural gas in Montana. He testified that a statement on page 522 of the report states, **A**Respondent, (respondent is Northwest Alaskan) receives natural gas from Pan-Alberta Gas, Ltd. at Kingsgate, British Columbia and Monchy, Saskatchewan, both on the US/Canadian border. The natural gas is delivered to US customers on the US side of the border (Idaho and Montana).@

Mr. Donkin stated that, for each of the years included in the audit period, the FERC form number two filings indicate the same point of delivery.(Tr III pg 17)

39. Mr. Donkin supported his testimony concerning the point of delivery by referring to the FERC form number sixteen, a required report that is an annual sales and requirements report. That form indicates that **A**delivery point@ for NWA customers in the US is **A**Morgan Port, Phillips County, and these are all in Montana.@ (Tr III pg 20)

40. Mr. Donkin stated that specification of title delivery point in purchase contracts is necessary because **A**regulatory requirements can be affected by where the point of delivery takes place. Jurisdictional issues can arise as to whether it's interstate or intrastate.@ (Tr III pg 29)

41. The NWA natural gas resale contracts with its customers passes the responsibility to arrange for transportation of the purchased gas and paying for the transportation on to the purchaser. (Ex J-12)

42. NWA is regulated under the Natural Gas Act. If NWA sold natural gas only outside the United States FERC regulation would not be required. FERC does have jurisdiction over the importation of natural gas.

43. Revenue Agent Brian Staley testified as to the audit at issue in this appeal. He stated one of the reasons the audit was performed is that, prior to the audit, ~~A~~the Williams Companies was filing separate company returns in the state of Montana. Each of their subsidiaries that had business was filing returns on a separate company basis under that separate company's name. And part of that audit was to go and determine if that was the correct filing method for these companies, or if they should be included in a unitary combined return and file just one return.@ (Tr IV pg 97)

There are other reasons for the audit that Mr. Staley explained: another subsidiary of Williams ~~A~~had an interest in the Northern Border pipeline@; for the years ~~A~~1987 through 1991 Northern Alaska Pipeline Company had filed and reported sales to Montana of a large amount, and in 1992 and 1993, the sales reported on those returns dropped to zero.@ (Tr IV pg 98)

44. The Williams Companies conceded to the fact of filing as unitary in a letter dated February 1, 1995 from David Wulf to Mr. Staley. (Post audit report)

BOARD-S DISCUSSION

The issue before this Board is whether Northwest Alaskan Pipeline Company, a wholly owned subsidiary of THE WILLIAMS COMPANIES, INC., has taxable nexus with the State of Montana, providing a basis for an assessment of additional taxes and interest as determined by the Montana Department of Revenue.

To determine the issue of nexus, NWA must have a connection or definite link with Montana, and the assessment levied must reflect NWA's activity in the state. One element central to that determination is where the transfer of the Canadian gas occurs.

At the hearing before this Board, the appellant argued that the purchase by NWA of the Canadian gas from Pan-Alberta, the import of that gas, and the transfer to Northern Border Pipeline occurred **A**simultaneously@ or in a **A**nanosecond@ or in a **A**dead zone@ between the United States and Canada; and a witness for the appellant stated: **A**The gas is sold on the international border, after export from Canada and before import to the United States.@

The Board rejects the idea that the transactions

occur simultaneously. The importer, NWA, imports gas prior to sale and, irrespective of the fact that the sale might occur immediately thereafter, NWA does indeed have possession for a period of time, whether that is for a nanosecond or some other period of time. There was no credible evidence presented to substantiate the proffered theory that the international border is a **A**dead zone@ in which the transactions occurred.

The appellant, Williams Companies, Inc. and subsidiaries, argues that one of its subsidiaries, specifically NWA, is not engaged in business in Montana. It supports that argument by reliance on its claim that NWA is not organized to, nor has it ever, made a profit. It follows that argument with the conclusion that, if NWA is not profitable, it is not subject to Montana Corporation License Tax.

NWA is a wholly owned subsidiary of Williams. Williams is also the parent of its wholly owned subsidiary, Northwest Border Pipeline Company. Northwest Border Pipeline Company owns 12.5% of the Northern Border Natural Gas Pipeline which enters Montana near the Port of Morgan, Montana.

Williams went to great length to establish the fact that NWA is not considered a shipper on the pipeline system in either Canada or the United States; and, of course, NWA does not need to be a shipper, since it is buying and selling the product, the seller and the purchaser would be considered the

shippers. The sales contracts make the purchaser responsible for the transportation of the gas, so the cost of transportation is not borne by NWA.

Without NWA and its import authority, there presumably would be no customers for Northwest Border Pipeline Co. or for the Williams natural gas business. Whether NWA itself makes a profit is a reflection of the structure under which it was established to operate. The appellant provided numerous witnesses to underscore the point that NWA was never established to make a profit. NWA's purpose is, however, to ensure there will be product available to meet its business related entities and its parent Williams' customers needs for natural gas.

The role of NWA in this large project cannot be defined by its profitability status. The authorization by FERC for NWA to import and resell up to 800,000 Mcf of natural gas per day places NWA in the primary position of the entity which, in fact, makes the remainder of the system and the business generated by it possible, necessary, and a reality. Without NWA in the present structure, there would not be the generation of further business activity down the line to U.S. customers.

The appellant argues that the actions of purchase-export and import-sell occur at a point that is neither in Canada or the U.S. NWA is subject to FERC regulation. FERC

authorizes NWA to import and resell natural gas. NWA is required to file reports monthly, semi-annually, and annually with the FERC. FERC would not have regulatory authority beyond the U.S. border. If the actions of NWA were, in fact, beyond the boundaries of the U.S., FERC would not have jurisdiction.

NWA is the first owner of the natural gas subject to FERC regulation and, as such, the transactions are recognized as occurring in FERC jurisdiction within the U.S. Because of geography it follows then that, if the transactions occur within the U.S., they are occurring in Montana.

NWA, being a wholly owned subsidiary of Williams, is controlled by Williams. Both parties made it clear that NWA has no property or payroll in Montana. Williams testified that NWA is not a shipper on the pipeline system and it argues, if NWA is not a shipper, it only follows that NWA has no gas in the pipeline. NWA does not need to be designated as a shipper because it sells the gas to pipeline customers who do pay for transportation of the gas.

If NWA has no gas in the pipeline at any point, at any time, then it presumably has nothing to sell. We know that is not the situation since the record is clear that NWA buys and sells natural gas. That is its function, its reason for existence, and without ownership of gas to sell it would definitely not be able to perform its function. If that

occurred, it would have substantial impact on its parent, The Williams Companies, Inc.

The relationship of Williams and NWA is clear in that an employee of Williams Gas Pipeline Central is also NWA's Manager of Operations. He confirmed that, while NWA has no employees, agents, or independent contractors in Montana, it does take title to Canadian gas. As has already been stated, we also know that NWA then sells that gas and gives up title to the purchaser.

The Corporation License Tax is not a sales or use tax. It is a license fee paid by those subject to the tax based on business activity within the state. Corporations created, organized, or existing under and pursuant to the laws, agreements, or declarations of trust of any state, county, or the United States...@ pay the tax only on that income attributable to Montana. The fact that NWA is directly controlled by the parent and is engaged in business in Montana makes it subject to the tax. Neither Williams nor NWA is operating as a mail order house for retail sales of various products. One product is bought by a major importer of that product and sold to its customers. Those business transactions occur in Montana. Where the product that was purchased in Montana is eventually destined does not negate that fact that these sales by NWA were made in Montana.

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CONCLUSIONS OF LAW

1. The State Tax Appeal Board has jurisdiction over this appeal. ' 15-2-302, Montana Code Annotated.

2. **15-31-101. Organizations subject to tax.** (1) The term "corporation" includes associations, joint-stock companies, common-law trusts and business trusts which do business in an organized capacity, and all other corporations whether created, organized, or existing under and pursuant to the laws, agreements, or declarations of trust of any state, country, or the United States.

(2) The terms "engaged in business" and "doing business" both mean actively engaging in any transaction for the purpose of financial or pecuniary gain or profit.

(3) Except as provided in 15-31-103 or 33-2-705(4) or as may be otherwise specifically provided, every corporation engaged in business in the state of Montana shall annually pay to the state treasurer as a license fee for the privilege of carrying on business in this state the percentage or percentages of its total net income for the preceding taxable year at the rate set forth in this chapter. In the case of corporations having income from business activity which is taxable both within and outside of this state, the license fee must be measured by the net income derived from or attributable to Montana sources as determined under part 3. Except as provided in 15-31-502, this tax is due and payable on the 15th day of the 5th month following the close of the taxable year of the corporation. However, the tax becomes a lien as provided in this chapter on the last day of the taxable year in which the income was earned and is for the privilege of carrying on business in this state for the taxable year in which the income was earned. (Montana Code Annotated)

3. **15-31-311. Sales factor for sales in this state.** (1) Sales of tangible personal property are in this state if:

(a) the property is delivered or shipped to a purchaser, other than the United States government, within this state regardless of the f.o.b. point or other conditions of the sale; or

(b) the property is shipped from an office, store, warehouse, factory, or other place of storage in this state and:

- (I) the purchaser is the United States government; or
- (ii) the taxpayer is not taxable in the state of the purchaser.
- (2) Sales, other than sales of tangible personal property, are in this state if:
 - (a) the income-producing activity is performed in this state; or
 - (b) the income-producing activity is performed both in and outside this state and a greater proportion of the income-producing activity is performed in this state than in any other state, based on costs of performance. (Montana Code Annotated)

4. 42.26.255 SALES OF TANGIBLE PERSONAL PROPERTY

(1) Gross receipts from the sales of tangible personal property (except sales to the United States Government; see ARM 42.26.256) are in this state:

(a) if the property is delivered or shipped to a purchaser within this state regardless of the f.o.b. point or other conditions of sale; or

(b) if the property is shipped from an office, store, warehouse, factory, or other place of storage in this state and the taxpayer is not taxable in the state of the purchaser.

(2) Property shall be deemed to be delivered or shipped to a purchaser within this state if the recipient is located in this state, even though the property is ordered from outside this state.

(3) Property is delivered or shipped to a purchaser within this state if the shipment terminates in this state, even though the property is subsequently transferred by the purchaser to another state. (ADMINISTRATIVE RULES OF MONTANA)

5. Based upon the foregoing testimony and evidence, this appeal is hereby denied and the decision of the Department of Revenue is hereby affirmed.

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ORDER

IT IS THEREFORE ORDERED by the State Tax Appeal Board of the State of Montana that the corporate assessment and interest as determined by the Department of Revenue is properly due and owing by THE WILLIAMS COMPANIES, INC. and SUBSIDIARIES.

Dated this 31st of December, 1998.

BY ORDER OF THE
STATE TAX APPEAL BOARD

(S E A L)

PATRICK E. McKELVEY, Chairman

GREGORY A. THORNQUIST, Member

LINDA L. VAUGHEY, Member

NOTICE: You are entitled to judicial review of this Order in accordance with Section 15-2-303(2), MCA. Judicial review may be obtained by filing a petition in district court within 60 days following the service of this Order.