

Denver Law Review

Volume 66
Issue 4 *Tenth Circuit Surveys*

Article 37

February 2021

Tax

Denver University Law Review

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Recommended Citation

Denver University Law Review, Tax, 66 Denv. U. L. Rev. 805 (1989).

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TAX

Southwest Public Service Co. v. Federal Energy Regulatory Commission, 842 F.2d 1204

Appellant Southwestern Public Service Co. appeals a Federal Energy Regulatory Commission (FERC) order requiring it to (1) retroactively change its method of accounting for investment tax credits from the “flow through” method to the “normalization” method; and (2) stop including accrued unbilled revenues in its rate base until it shows these revenues are legally collectible. Reversed in part, affirmed in part.

The court of appeals noted that the FERC had issued no directives or guidelines relating to investment tax credits prior to the order requiring the retroactive accounting change. Because of this, the court invalidated the accounting ruling on the grounds the FERC had abused its discretion under the 1971 Revenue Act. The court did uphold the FERC’s ruling requiring a showing of collectibility before accrued unbilled revenues could be included in Southwestern’s rate base.

United States v. Bell Credit Union, 860 F.2d 365

Appellant credit unions appeal a district court decision allowing the I.R.S. to levy the credit union share accounts of individual taxpayers. Affirmed.

In affirming, the court of appeals noted that only two defenses will justify a third party’s refusal to comply with an I.R.S. levy; (1) the third party does not possess the property, or (2) the property is subject to a prior judicial attachment or execution. The credit unions failed to establish either of these defenses.

Freede v. Commissioner of Internal Revenue, 864 F.2d 671

The Commissioner appeals from a decision in favor of the taxpayers which held that disputed excess payments created “production payments” within the meaning of the Internal Revenue Code, 16 U.S.C. § 636(a), and as such, were to be treated as nontaxable loans. The Commissioner sought reversal, arguing that the excess payments should have been included as taxable income in the year received. Reversed.

Taxpayers own fractional working interests in various oil and gas leases in Oklahoma. In 1975 and 1976 they contracted with Oklahoma Gas and Electric Company (“OG & E”) whereby OG & E agreed to pay for a specified minimum quantity of gas each year without regard to actual delivery of the gas. If the amount of gas paid for under the “take or pay” provision exceeded the amount of gas actually received, OG & E had the right to credit the excess amount in later years against gas taken in excess of the minimum contract quantity. The taxpayers did not in-

clude the amounts received in 1979 for gas not taken in that year as income.

In order for OG & E's right of recoupment to qualify as a production payment under § 636(a), five criteria must have been met. On appeal, the Commissioner challenges only one of these criteria — that OG & E's recoupment right constituted an "economic interest" in the minerals in place. Under *Palmer v. Bender*, 287 U.S. 551 (1933), a two-part test is used to determine whether an economic interest exists. Under the first prong of the test, this court found that OG & E has only an arguable economic interest in the minerals in place, but that no conclusion need be drawn, since OG & E's recoupment right clearly fails the second prong of the *Palmer* test, as OG & E has not made any investment in the gas producing enterprise and does not look to income derived solely from extraction of the mineral for the return of any investment. The result is that OG & E's interest is clearly one of a consumer, not one of an investor. Thus, this court found that OG & E's interest was an "economic advantage" rather than an "economic interest" as set forth in *Helvering v. Bankline Oil Co.*, 303 U.S. 362 (1938). Furthermore, OG & E is not seeking, through its recoupment right, a profit from the extraction of gas. The possibility of profit that is dependent solely on the extraction and sale of a mineral is essential to the existence of an economic interest. Therefore, the excess payments did not create production payments for § 636(a) purposes and is to be included in taxpayers' income in the year received.