

**CONSERVATION DEPARTMENT: Oil and Gas Leases.**  
**OIL AND GAS: Severance and Privilege Taxes.**  
**LEASES: Shifting of Tax Burden.**  
**TAXATION: Severance and Privilege Taxes.**

State of Michigan Conservation Department oil and gas leases make no provision for shifting of the tax burden as to severance and privilege taxes to the State for the  $\frac{1}{8}$  of the oil specified as royalty.

Severance and privilege taxes are the primary liability of the producers of oil and they must pay these taxes on the entire amount of the oil produced and may not deduct  $\frac{1}{8}$  of these taxes from the State's royalty in the absence of statutory authority.

A division order cannot make the State of Michigan liable for severance and privilege taxes when these, by statute, are made the primary responsibility of the producer.

The State of Michigan is entitled to receive full  $\frac{1}{8}$  royalty under its lease without deduction for any taxes.

No. 4160

June 17, 1963.

Mr. Gerald E. Eddy, Director  
 Department of Conservation  
 Mason Building  
 Lansing, Michigan

This is in response to your letter of March 13, 1963. You indicate that questions have been raised by State auditors concerning the State's royalty interest in oil and gas under State leases. The questions concern the industry practice of withholding a severance tax of 2% of the gross cash market value of the product<sup>1</sup> and of a privilege tax of  $\frac{1}{8}$  of 1¢ per barrel of crude oil<sup>2</sup> from proceeds paid to the State. You ask whether these taxes are rightfully imposed on the State's proportionate share of all oil and gas produced and sold, and as to the legality of imposing a tax on the State's share of production.

Enclosures submitted are State of Michigan lease form and Division Order form.

Act 48, P.A. 1929, Sec. 1,<sup>3</sup> provides in part as follows:

"There is hereby levied upon each corporation, association, or person engaged in the business of severing from the soil oil or gas, a specific tax to be known as the severance tax. \* \* \*"

It would appear from the above quoted statute that the producer or the party engaged in withdrawing the oil and separating it from the ground is the party upon whom the severance tax is levied. In other words, this is a specific tax.

Section 3<sup>4</sup> of the act provides in part:

<sup>1</sup> Act 48, P.A. 1929, M.S.A. Sec. 7.351, C.L. 1948, Sec. 205.301 et seq.

<sup>2</sup> Act 61, P.A. 1939, as amended, M.S.A. Sec. 13.139(22), C.L. 1948, Sec. 319.22.

<sup>3</sup> C.L. 1948, Sec. 205.301 et seq.; M.S.A. 7.351.

<sup>4</sup> M.S.A. 7.353; '48 C.L. 205.303.

"The severance tax required to be paid by each producer at the time of rendering each monthly report, or by any pipe line company, common carrier or common purchaser, for and on behalf of any such producer, shall be in the amount of two (2) per cent of the gross cash market value of the total production of such oil or gas during the preceding monthly period. The value of all such production shall be computed as of the time when and at the place where the same have been severed or taken from the soil immediately after such severance. Except as otherwise provided in this section, the payment of said severance tax shall be required of the severor or producer actually engaged in the operation of severing the oil or gas. \* \* \*

A privilege tax is imposed by Act 61, P.A. 1939<sup>5</sup> and provides as follows:

"A privilege fee of one-eighth ( $\frac{1}{8}$ ) of 1 cent per barrel shall be paid upon oil produced in Michigan and sold. This fee shall be levied and collected by the Michigan tax commission in the same manner as provided in and by Act No. 48 of the Public Acts of 1929, of the state of Michigan. All moneys received from this source shall be turned in to the general fund of the state."

We will first consider the industry practice of withholding a severance tax of the gross cash market value of the product. Our research discloses that a number of oil and gas producing States have enacted statutes levying production, severing, occupation, privilege and distribution taxes on gross productions of oil and gas. Examination of the work entitled "Summers on Oil and Gas," Section 801, page 410 indicates that the practice varies as to who bears the tax and he says as follows:

"\* \* \* In some states the burden of the tax is borne by the lessee and royalty owner proportionately, but in others it is borne by the lessee or producer alone. In some states such taxes are in lieu of property taxes, but in others they are additional taxes."

The Michigan acts levying the severance and privilege taxes have not been judicially construed.

Examination of the State of Michigan lease furnishes no indication that the taxes imposed by the above statute are to be borne by the State of Michigan. The State of Michigan lease makes the following provisions for payment of royalty:

"F(1a) To deliver to the credit of the Lessor herein, free of cost in tank car, or pipe line to which Lessee may connect its well or wells, the equal one-eighth part of all oil produced and saved from the leased premises described above and listed in Schedule \_\_\_\_\_, or at the option of the Lessor, Lessee shall pay the value thereof in cash at the prevailing market price of oil of same grade and quality at that time and place.

"(2) Should gas and oil both be found in any well, the Lessee shall pay to the Lessor for gas produced and sold from any such oil well, as royalty, one-eighth of the value thereof in cash at the prevailing market price in the field where produced. If such gas is used by the Lessee for

<sup>5</sup> C.L. 1948, Sec. 319.22; M.S.A. 13.139(22).

the production of casinghead gasoline, the royalty shall be one-eighth of the gross proceeds received from the sale of such casinghead gasoline and one-eighth of the gross proceeds received from the sale of gas from which the casinghead gasoline has been extracted; provided further that the Lessor shall receive as royalty one-eighth of the gross proceeds of the sale of drip gasoline and natural gasoline recovered from the gas produced from leased premises."

No arrangement is made in any of the clauses contained in the lease for the shifting of the tax burden on the  $\frac{1}{8}$  royalty interest of the State.

You have furnished us with a copy of a typical Division Order entered into by an oil company and the Department of Conservation. This Division Order makes a provision for payment of taxes in paragraph 6 which reads as follows:

"6. You are hereby authorized at your election to withhold from the proceeds accruing hereunder to any of the undersigned the amount of any severance, production, occupation or other tax levied against him by or under authority of the laws of the United States and of the State of Michigan for and on account of his interest in said oil, land or lease and to pay such tax or taxes with the withheld proceeds."

We do not consider that this Division Order can impose any tax liability where none exists. A Division Order is entered into for the purpose of separating the various interests and to determine how payments shall be made in satisfaction of royalties. The agreement between the Lessor and Lessee is contained in the lease and determines the various liabilities. A lease is not affected by the Division Order. *Stanolind Oil & Gas Co. v. Terrell*, (Tex.), 183 S.W. 2d 743.

Under the Michigan acts, the privilege tax is imposed upon the severor or producer. There is authority to the effect that by statute or by agreement the shifting of this tax can be made to the Lessor. However, that is not the situation here. The lease with the State of Michigan does not provide for the assumption of the tax burden by the State of Michigan and if it did, such a provision would be invalid in the absence of statutes permitting the same.

The General Property Tax Law provides in part:<sup>6</sup>

"Property exempt from taxation.] Sec. 7. The following property shall be exempt from taxation:

\* \* \*

State property.] Second, All public property belonging to the state of Michigan, except licensed homestead lands, part-paid lands held under certificates, and lands purchased at tax sales, and still held by the state;"

In the case of *Ryerson v. Township of Laketon*,<sup>7</sup> it is stated:

"When a tax is levied for any purpose, it must have express warrant of law to authorize its imposition."

<sup>6</sup> M.S.A. § 7.7; 1948 C.L. § 211.7.

<sup>7</sup> 52 Mich. 509, 517.

and in *People v. Ingalls*,<sup>8</sup> it is stated:

“The doctrine has been pretty well settled in this State and elsewhere that property owned by the State or by the United States is not subject to taxation unless so provided by positive legislation. \* \* \*”

I am of the opinion that the State's 1/8 royalty interest is due and payable to the State of Michigan without any withholding for severance or privilege taxes.

FRANK J. KELLEY,  
*Attorney General.*

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**LEGISLATURE:** Members disqualified as candidates for other state offices.

**CONSTITUTIONAL LAW:** Legislators disqualified as candidates for other state offices.

A member of the legislature is prohibited by Article IV, Section 9, of the 1963 Constitution from receiving an appointment, and is disqualified from election to another state office, the term of which is to commence during his term of office as a member of the legislature. Such prohibition or disqualification is not applicable to a local office.

No. 4169

June 17, 1963.

Honorable Joseph A. Gillis  
State Representative  
2312 Guardian Building  
Detroit 26, Michigan

Your letter cites Article IV, Section 9, of the Revised Constitution, and requests my opinion on the following question:

“May a member of the Legislature run for another State or Local Office while serving in the Legislature under the revised Constitution?”

Reference will first be made to the predecessor of such section in the 1908 Constitution, i.e., Article V, Section 7, which read in part:

“No person elected a member of the legislature shall receive any civil appointment within this state or to the senate of the United States from the governor, except notaries public, or from the governor and senate, from the legislature, or any other state authority, during the term for which he is elected. All such appointments and all votes given for any person so elected for any such office or appointment shall be void. \* \* \*”

The corresponding provision of the 1850 Constitution, i.e., Article IV, Section 18, read practically the same, aside from the exception inserted in the 1908 section relating to notaries public.

<sup>8</sup> 238 Mich. 423, 425. See also: *Wyandotte v. State Board*, 278 Mich. 47; O.A.G. 1959-1960, Vol. 1, pp. 201, 202, No. 3437; O.A.G. 1961-1962, pp. 597, 598, No. 4095.