



## Texas: State Supreme Court affirms constitutionality of heavy equipment appraisal statute

TAX AND BENEFITS CHALLENGES | MAY 10, 2018

Article 8 of the Texas Constitution, which covers taxation and revenue matters, provides that “[t]axation shall be equal and uniform,” and that property “shall be taxed in proportion to its value.”

So begins the opinion in the Texas Supreme Court, in the case *EXLP Leasing LLC et al. v. Galveston Central Appraisal District*, in which the court sided with the petitioner leasing companies, and held that the statutory formula that they used to calculate the taxable value of leased natural-gas compressors is constitutional.

### BACKGROUND

The dispute between the leasing companies on one hand, and the Galveston County appraisal district on the other, focused on the constitutionality of the Texas statute that provides the formula at issue. Also at issue was which county could tax the inventory.

The court’s opinion provides the background details as follows. The petitioners, EXLP Leasing, LLC, and EES Leasing, LLC (collectively, “EXLP”) are wholly owned subsidiaries of Exterran Holdings, Inc. EXLP owns and leases out compressor stations, which are used to deliver natural gas into pipelines. Some of these compressors are used in Galveston County.

Until 2012, Galveston County taxed the compressors as business-personal property based on their full market value. This changed when the legislature added leased heavy equipment to the statutory formula used to appraise the value of heavy equipment held by dealers for sale. The new formula, set forth in Tex. Tax Code § 23.1241(b), requires appraisal based on the lease revenue the compressors generated during the previous tax year, divided by twelve.

EXLP was pleased with this change, contending that lawmakers intended to fix a problem that arose when the same equipment was leased multiple times within one year, with each lease counting as an individual sale for tax purposes. Citing the legislation’s fiscal note, the Texas Supreme Court noted that lawmakers thought that their new formula would simplify the appraisal process, and provide counties with an “offsetting gain” for the tax revenue they stood to lose.

The county, on the other hand, argued that not only was there no offset, the statutory change caused a 97 percent loss in its compressor-based tax revenue.

The 2012 amendment to the statute also triggered a dispute over which county the compressors should be taxed in. EXLP urged that even though the compressors were located in Galveston County, they should be taxed in Washington County, because, as directed in the statute, that is where EXLP maintained its business address and storage yard.

Ultimately, the court held that Galveston County failed to rebut the presumed constitutionality of the statutes at issue, and that Washington County is the taxable situs for the compressors.

### THE COURT’S ANALYSIS

Quoting its own case law precedent, the court observed that “[t]here is always a presumption of constitutional validity with regard to legislation and it is especially strong in respect to statutes relating to taxation.” This is based on another presumption, that “the Legislature understands and correctly appreciates the needs of its own people, that its laws are directed to problems made manifest by experience, and that its discriminations are based upon adequate grounds.” Thus, it fell to Galveston County to prove the enactment’s unconstitutionality.

The underpinning of the county’s position was that the statutory formula “values the compressors for tax purposes at ‘a minute fraction’ of their market value,” and that it is the market value that the constitutional provision refers to in the requirement that that property be taxed “in proportion to its value.”

But the court took the position that there is nothing in the constitution that “binds the legislature to tax only on ‘market value.’” The court opined that to read that document as the County would have it do “would both add a word the drafters omitted and reduce legislative discretion...”

Much of the court’s rationale centered on references to case law involving special appraisal provisions, and the freedom that the legislature has “to adopt the mode of ascertaining the value of any class of property by such method as it might deem best.”

To the county’s argument that the outcome is unfair, the court simply stated that an unfair outcome “is a concern beyond our purview. Even if the policy is inadvisable, we decline to usurp legislative authority by issuing reform diktats from on high, supplanting lawmakers’ policy wisdom with our own.” Leeway to the legislature similarly applied to the county’s point that the valuation formula was “fundamentally inequitable” in violation of the constitution’s equal and uniform provision, “so long as the classifications are not unreasonable, arbitrary, or capricious.”

With respect to the other question, which county is the correct taxable situs, the court once again looked to the language of the 2012 statutory amendment, and acknowledged that “taxes should be paid in the county where [a company] conducts business;” the legislature provided only for limited exceptions, none of which were relevant in this case.

### IMPLICATIONS

At issue was more than \$66 million in aggregate tax benefits that accrued to EXLP. In its announcement praising the court for its decision, the law firm handling the case divulged that it has filed more than 800 similar suits since 2012, against more than 100 appraisal districts, for their alleged failures to apply the statute correctly. After the court issued this opinion, the firm declared that it the outcome is especially important because the legislature retained its rightful flexibility and authority, which necessarily calls for accounting for changes that come

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from "new technology, new forms of property, new economic realities, and the needs of the Texas people."

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