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Arkansas Ad Valorem Mineral Taxes: An Overview with Related Title Problems

By

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I. Introduction

The Arkansas Constitution requires ad valorem taxes on all real and personal property in the state, save for exempt property.² Ad valorem taxes are over and above the severance tax.³ All real property interests related to producing minerals, whether fee, royalty, working, or overriding, are subject to ad valorem taxation.⁴

There are no fewer than 370 reported cases in Arkansas regarding tax sales.⁵ This presentation is not exhaustive of all tax title topics, but will cover the essentials of ad valorem taxation of minerals and issues important to leasing and title examination.

This article first examines Arkansas's ad valorem taxation system as applied to mineral interests, reviewing assessment and valuation laws for mineral interests. Next is an overview of the process of enforcing tax delinquencies on mineral interests. This article then examines classes of title defects for tax minerals. Finally, there is a short and modest proposal for reform to increase the marketability of mineral tax titles.

II. The Assessor, Taxation Process, and Enforcement Process

A) The Assessor's Role, Valuation, and Taxation

It is the duty of the County Assessor to inventory and value all lands within the subject County. The Assessor is to account for every parcel of real property and to note

¹ Questions regarding this presentation may be sent to the author at mrobinette@perkinstrotter.com; a pdf of this article is available at <http://www.perkinstrotter.com/articles/index.htm>. The author wishes to thank both his colleagues at his firm and among the oil and gas bar for their efforts in shaping this article.

² Ark. Const. Ann. Art. 16 § 5 (“all real and tangible property subject to taxation shall be taxed according to its value, that value to be ascertained in such manner as the General Assembly shall direct, making the same equal and uniform throughout the State.”); *See also* Ark. Const. Amend. 71.

³ ACA § 26-58-103 & 26-58-109.

⁴ *See* State Attorney General v. Arkansas Fuel Oil Co., 179 Ark 848, 18 S.W.2d 906 (1929); *See also* ACA § 26-36-212 (giving taxing units the ability to sue working interest, royalty, or overriding royalty owners for delinquent ad valorem taxes).

⁵ This is a conservative estimate based on a search conducted January 30, 2010, of the Arkansas cases database on Westlaw.com for “Sale of Land for Nonpayment of Tax” in the headnotes of the opinion. This number does not reflect Federal cases dealing with Arkansas law.

which properties are exempt from taxation.⁶ To accomplish this, the statutes mandate that each person owning property provide a verified listing of all real and personal property.⁷ For severed minerals, the statutes mandate that the Assessor assess severed minerals whenever mineral severances are recorded or whenever the Assessor has personal notice of the severance.⁸ The statutes further empower the Assessor to cause any person “to answer upon oath and furnish proof demanded” for any type of information “pertaining to the location, amount, kind, and value of his own property or that of another person.”⁹ Failing to comply with the Assessor’s request can result in prosecution with a fine not less than \$10 and not more than \$100,¹⁰ and the Assessor “shall assess such persons a per capita or poll tax” for failing to file a property schedule, failing to truly value an item thereon, or omitting any it of property from the property schedule.¹¹

It is the Assessor’s duty to appraise all real property, including minerals, by July 1 of the appraisal year.¹² Each county must appraise property every 3 or 5 years, depending on how fast property values rise.¹³ Severed mineral interests are subject to separate assessment and valuation.¹⁴ The statutes allow the Assessor to list mineral rights separately or with the related surface interest.¹⁵ Because Arkansas has a system of equalization, the Assessor must not engage in intentional or systemic discrimination between owners of the same class of property.¹⁶

Because nearly all minerals are underground, it is very difficult, if not impossible, to properly appraise their value. The General Assembly directs that all non-producing minerals have zero value¹⁷ while the Assessment Coordination Department (ACD) of the Arkansas Public Service Commission has the duty to promulgate rules for valuation of producing minerals.¹⁸ These rules are to be in accordance with market value.¹⁹

⁶ ACA § 26-26-718.

⁷ ACA § 26-26-501; §§ 26-26-902-903. The property owner is relieved from this duty if the Assessor uses a listing from a prior year. This is ordinarily the case.

⁸ ACA § 26-26-1110(a)(1). It is interesting that the Assessor has a general duty under § 26-26-718 to account for every parcel of real property, yet it appears that the Legislature may not intend for severed minerals to fall under the same rigorous accounting due to § 26-26-1110. This raises interesting Constitutional questions. Because the Arkansas Constitution requires equalization, generally exempting the Assessor from accounting for all mineral interests could violate the Equal Protection Clause of the Constitution. *See e.g. Allegheny Pittsburgh Coal Co. v. Webster County Commission*, 488 U.S. 336 (1989).

⁹ ACA § 26-26-910 (b)(2).

¹⁰ ACA § 26-26-912(b).

¹¹ ACA § 26-2-104.

¹² ACA § 26-26-1101.

¹³ *See* ACA §§ 26-26-306-308 and 26-36-410. The triggering events for county-wide reappraisal are beyond the scope of this presentation.

¹⁴ ACA § 26-26-1202(h).

¹⁵ ACA §§ 26-26-1111-1112.

¹⁶ *See* *Allegheny Pittsburgh Coal Co. v. Webster County Commission*, 488 U.S. 336 (1989). *See also* note 2, *supra*.

¹⁷ ACA § 26-26-1110(c).

¹⁸ *Id.* at (c)(4).

¹⁹ ACA § 26-26-1202.

The current ACD rules for valuing and assessing mineral rights published in 2006²⁰ divide minerals into four categories: Non-producing Minerals, Mining, Producing Oil Wells, and Producing Gas Wells. These rules do not reflect the 2009 statute change regarding non-producing rights. Non-producing minerals are not subject to valuation by declaration of the Legislature. It is also noteworthy that a non-producing mineral lease is not subject to valuation or even assessment.²¹

The ACD rules for mining land valuation are to add:

1. The land according to its capability classification (e.g. residential, pasture, timber, agricultural, etc.)
2. All improvements and fixtures appurtenances on the lands, such as buildings, roads, and all other improvements of a permanent nature.
3. The mineral deposit as it is rendered by the owner and/or the operating company when the amount rendered is in conformity with the Assessor's valuation.

Presumably, the owner/operator "rendition" of the mineral deposit's value would deduct the royalty interest, the expenses to extract the deposit, and would reflect the operator's market price for the mineral.

The ACD rules value a royalty interest in mining land by multiplying an estimated value of the mineral from the Arkansas Geological Commission by the royalty rate less "necessary expenses." The rules do not elaborate on what are "necessary expenses" or on what gross basis to multiply the royalty rate (e.g. all of the mineral in place or the minerals produced in the taxing year). Once the Assessor reaches a valuation for either land or royalty, the assessed value is simply the valuation multiplied by 20% to arrive at the value for taxation.

For Oil wells and Oil Royalty, the ACD rules first divide the producing oil well into a Production Class. As the well's production capacity increases, so does the well's tax burden. Based on assumptions of the price of oil as \$36.12/bbl, a depletion rate of 30% for bottomhole wells and 20% for strippers, and a discount factor of 15%,²² the ACD assigns an "amount per barrel" each production class of well. The value for taxation is the product of the amount per barrel, average daily production in barrels, and the interest of entity taxed. The last variable is the net revenue of each respective owner (Working Interest, Overriding Interest, and Royalty Interest).

²⁰ See Appendix 1, *infra*.

²¹ See Arkansas Attorney General's Opinion No. 85-133.

²² Note this "discount rate" is not the 20% stated for mining and oil lands. The ACD rules utilize a "discount rate" which appears to be equalization percentage. Assessments cannot use more than 20% of the true market value of the property as an equalization percentage. ACA §26-26-303.

The rules state that the working interest may be subject to a “Water Flood” adjustment of up to 25% and an “Enhanced Recovery” adjustment of up to 50%.²³

The rules value producing gas interests begin with an assumption of \$6.19 per M.C.F. multiplied by 365 days for an annual value of \$2259 per M.C.F. per day. The valuation for assessment is the product of the annual value and the quantum of net revenue interest held by the interest (Working, Royalty, or Override) less 13% for expenses times the average daily production.²⁴ From there, the rules apply a discount rate of 20% to arrive at the assessed valuation.

The rules instruct that the assessor may adjust the annual value if the contract pricing is higher or lower than \$6.19 per M.C.F. In that case, the assessor is to retain a copy of the contract to verify the contract price.

Additionally, the rules instruct the Assessor to obtain a division order for each oil and gas unit, and if the operator fails to provide the division order, the assessor should assess 100% of the production against operator.²⁵

Following the appraisal of the mineral interest, the Assessor must notify the taxpayer of the valuation no later than 10 business days past July 1 of the appraisal year.²⁶ A mineral, royalty, or working interest owner may appeal their assessed value to the County’s Board of Equalization,²⁷ County Court,²⁸ and finally to Circuit Court.²⁹ After 10 business days past July 1 of the tax year, the Assessor’s duties for the year end.

The timeline for tax assessment and collection is as follows:

1. Lien arises on first Monday of January, year 1.³⁰

²³ The rules do not state a basis for either adjustment, but the basis may be the severance tax credits found at ACA § 15-72-1001 and ACA § 26-58-201 et. seq., respectively. The author could find no other basis in either the ACD rules or the code. If the ACD’s rules do in fact draw from these statutes, they are probably without authority to apply the adjustments because the statutes clearly apply to severance taxes, not ad valorem taxes which are separate and above severance taxes. See ACA § 26-58-103 & 26-58-109.

²⁴ The rules do not explicitly state that the Assessor should determine the average daily production, but the rules do cache the product of the annual value per M.C.F., working interest percentage, expense reduction percentage, and discount factor as “Assessment Value per M.C.F. Average Daily Production.” This implies the Assessor’s next step is to multiply the average daily production by this number. The rules do not instruct the Assessor to do so.

²⁵ The author found no basis for the assessor to inflict this type of penal assessment, other than the “per capita or poll tax” for failing to list property authorized by § 26-26-912. There is no case law or other statute explaining this Assessment power. Obviously, a poll tax is Unconstitutional under the 14th Amendment of the U.S. Constitution. The “per capita” tax, as a term of art, is simply a flat tax levied against an individual. This instruction by the ACD could lead to complicated situations where the mineral owner winds up forfeited without notice due to an operator’s unauthorized 8/8 assessment.

²⁶ ACA § 26-23-203.

²⁷ An appeal of the Assessor’s valuation must occur by the 3rd Monday of August, year 1. ACA § 26-27-317.

²⁸ ACA § 26-27-318.

²⁹ *Id.*

³⁰ ACA § 26-34-101.

2. Assessor appraises real property by July 1 of year 1.³¹
3. Assessor notifies property owner of value not later than 10 business days past July 1 of year 1.³²
4. Clerk assumes control over assessment rolls, 3rd Monday of August, year 1.³³
5. School districts hold elections 3rd Tuesday of November of year 1 to set school millage rate.³⁴
6. City Council levies general millage rate prior to November of year 1 meeting of quorum court.³⁵
7. Quorum Court levies millage rates at November of year 1 meeting.³⁶
8. After November of year 1 levy, Clerk begins extending taxes and preparing tax book.³⁷
9. Third Monday of February, year 2: Clerk finishes extending taxes and preparing book, then delivers book to collector with warrant authorizing collection of taxes attached.³⁸
10. Taxes are due and payable first business day of March, year 2.³⁹ Collector begins mailing tax statements, but must do so before July 1 of year 2.⁴⁰
11. Property owner must pay taxes by October 10, year 2.⁴¹

Failing to pay taxes by October 10, year 2 begins the process of enforcement.

B) Enforcement of Delinquent Ad Valorem Taxes

Arkansas uses a system of statutory forfeiture procedures to enforce non-payment of delinquent ad valorem taxes. Historically, there were two major statutory forfeiture and sale procedures in effect. The first, from statehood to 1983, allowed the county to sell the tax-forfeited lands prior to forfeiting the land to the state. Because courts easily found

³¹ ACA § 26-26-1101.

³² ACA § 26-23-203.

³³ ACA § 26-26-716.

³⁴ ACA § 6-14-102.

³⁵ ACA § 26-73-202.

³⁶ ACA § 14-14-904.

³⁷ ACA § 26-28-103.

³⁸ ACA §§ 26-28-103 and 26-28-108, respectively.

³⁹ ACA § 26-36-201.

⁴⁰ ACA § 26-35-705.

⁴¹ ACA § 26-35-501.

fault with the county officials' conduct in selling the property, the Legislature completely overhauled the tax forfeiture statutes by Act 626 of 1983 to remove the county from the process. Under Act 626, the state took control of the selling forfeited land via the Commissioner of State Lands (COSL). Because all pre-1985 forfeitures of severed minerals are void,⁴² this presentation will only address the post-1985 statutory scheme.

The current tax forfeiture process, based on Act 626 of 1983 and subsequent amendments, is as follows:

1. The Collector publishes list of delinquent properties in legal newspaper of County.⁴³
2. If property taxes aren't paid, the land remains on the tax books as delinquent until October 10, year 3.⁴⁴ The delinquent property owner may redeem the property with the Collector at any time during the year.⁴⁵
3. Between September 1 and October 10 of year 4, the collector publishes a list of the delinquent property in the newspaper of general circulation.⁴⁶
4. Prior to certification to the State, the Assessor verifies certain facts.⁴⁷
5. Prior to certification to the State, the Collector verifies the amount of delinquent lands being equal to the credit allowed the Collector on the current tax settlement, and the Collector records a certified list of property in the county real estate records.⁴⁸
6. October 10, year 4, the land forfeits to the state for unpaid taxes.⁴⁹

For severed minerals, the statutes mandate a different set of rules than for the disposal of surface estates as embodied by Act 864 of 1993:⁵⁰

⁴² See Section III(2)(i), *infra*.

⁴³ ACA § 26-37-107.

⁴⁴ ACA § 26-37-101.

⁴⁵ ACA § 26-37-109.

⁴⁶ ACA § 26-37-103.

⁴⁷ ACA § 26-37-103.

⁴⁸ ACA § 26-37-106. Formerly, this requirement had to occur prior to the sale. Because the county Collector no longer sells tax-delinquent properties and the last published case construing this section was for a sale that occurred prior to the 1983 act prohibiting county sales, it seems likely a court construing this requirement would place the timing prior to the certification to the state. Prior to 1993, the Collector had to attach a certificate that stated various facts regarding publication. This was a fertile source of void sales, so the Legislature removed the requirement for an attached certificate of the Clerk. See e.g. *Broadhead v. McEntire*, 19 Ark.App. 259, 720 S.W.2d 313 (1986).

⁴⁹ ACA § 26-37-101.

⁵⁰ The Legislature acted quickly after the *Jones v. Flowers* decision, enacting extra notice procedures to satisfy Due Process for surface interests. The Legislature either inadvertently or intentionally overlooked the differing notice standards for severed minerals. One would believe this was an oversight given the obscurity of the separate mineral sale statute. For a discussion of the problems associated with the differing

1. The COSL notifies the “record owner” of the fact of forfeiture by certified mail to the record owner’s last known address.⁵¹
2. The COSL holds the property for one year without selling the property.⁵²
3. After the expiration of one year, the COSL holds the interest indefinitely until either the true owner redeems or the surface owner purchases the interest from COSL.⁵³

In addition to changing the disposition of mineral interests, the 1993 Act gave the surface owners the exclusive right to purchase the interests after the redemption period when at least 25% of the mineral interest was owned by one person, a group of persons related in the first degree of consanguinity, or a single legal entity. By Act 1279 of 2003, the Legislature enhanced the incentives for surface owners to purchase mineral rights by removing the 25% requirement and not requiring the surface owner to pay interest or penalties owed.

The incentive for the surface owner to purchase could work an unintended result. It is a well-settled rule that one cannot gain title of one’s co-tenants at a tax sale.⁵⁴ Thus, it is an open question as to what happens when a surface owner who also owns minerals purchases the tax title of his fellow mineral co-tenant. Under existing case law, such a purchase could be treated as a redemption in favor of all co-tenants with the surface owner having a claim against his fellow mineral co-tenant for the money spent to redeem the interest. If, on the other hand, the surface owner owned no minerals, the effect of the statute differs vastly. The surface owner simply becomes a mineral owner.

A more interesting possibility goes as follows: 1) Surface owner owns no minerals; 2) Surface owner buys 1/8 interest from the COSL; 3) Surface owner then buys the remaining 7/8 interest from the COSL. In this situation, the existing case law could work a strange result. The first 1/8 would be owned outright by the surface owner, but the remaining 7/8 would be a redemption in favor of the original owner of the 7/8 interest. This was probably not the Legislature’s intent, but a significant possibility that court will interpret the statute’s effect this way exists.

notice requirements, *See* Drew T. Sadler, Note, MINERAL RIGHTS? THE CONSTITUTIONAL DEFICIENCY OF SECTION 26-37-314 OF THE ARKANSAS CODE, 62 Ark. Law. Rev. 611 (2009).

⁵¹ ACA § 26-37-314(a)(2).

⁵² *Id.* at (b)(2) and ACA § 26-37-301(a)(2).

⁵³ ACA § 26-37-314(a)(3)(A) and (b)(1).

⁵⁴ *See e.g.* *Hollway v. Berenzen*, 208 Ark. 849, 188 S.W.2d 298 (1945).

III. Tax Title Defects

No document of purported legal dignity has been treated more ignominiously by the legal profession than the tax-sale deed.⁵⁵

--Harvard Law Review, 1948

Prior to exploring title defects that occur with tax deeds, it is necessary to examine whether there is an effective statute of limitation that cures defective tax titles. After the sale, there are two statutes of that can affect the marketability of an interest obtained at a tax sale. The first, found in Title 18 of the Arkansas code, abbreviates the statutory period of adverse possession from 7 years to 2 years for those under possession by a tax deed.⁵⁶ The relevant⁵⁷ text follows:

No action for the recovery of any lands or for the possession thereof against any person, or his or her heirs or assigns, who may hold such lands by virtue of a purchase thereof at a sale by the collector or Commissioner of State Lands, for the nonpayment of taxes, or who may have purchased them from the state by virtue of any act providing for the sale of lands forfeited to the state or the nonpayment of taxes, or who may hold the land under a donation deed from the state, shall be maintained unless it appears that the plaintiff, his or her ancestors, predecessors, or grantors were seized or possessed of the lands in question within two (2) years next before the commencement of the action.

This statute is not applicable to severed mineral interests because of the possession element of the statute. Under Arkansas law, one must actually produce minerals to adversely possess them.⁵⁸ Unless the tax deed holder can convince an operator to risk a well on a tax deed for two years, this probably won't happen with an oil and gas interest.

The second statute of limitation, found in Title 26 of the code and enacted by Act 626 of 1983, then significantly amended by Act 791 of 1993 and Act 1036 of 2007 provides:

26-37-203. Contest actions

(a) If the tax-delinquent land is not redeemed within the thirty-day period, the Commissioner of State Lands shall issue a limited warranty deed to the land.

(b)(1) Except as provided in subdivisions (b)(2) and (3) of this section, all actions to contest the validity of the conveyance shall be brought within one (1) year after the date of the conveyance or thereafter be barred.

(2) A cause of action by a person suffering a mental incapacity, a minor, or a person serving in the United States armed forces during time of war during the two-year period shall be brought

⁵⁵ Note, THE CURRENT STATUS OF TAX TITLES: REMEDIAL LEGISLATION V. DUE PROCESS, 62 Harvard Law Review 93 (1948).

⁵⁶ ACA §§ 18-60-212(a) and 18-51-106(a).

⁵⁷ Both statutes contain this provision, but ACA § 18-60-212 contains additional procedures to set aside the tax sale.

⁵⁸ See Hurst v. Rice, 278 Ark. 94, 99, 643 S.W.2d 563, 565 (1982).

within two (2) years after the disability is removed, the minor reaches majority, or the person is released from active duty with the armed forces.

(3) An action to challenge the conveyance to a purchaser of land that was sold at a negotiated sale under § 26-37-101 shall be brought within ninety (90) days after the date of the conveyance or thereafter be barred.

(c) No deed issued after January 1, 1987, by the Commissioner of State Lands shall be void or voidable on the ground that the county did not strictly comply with the laws governing tax-delinquent land if prior to the issuance of the deed the Commissioner of State Lands complied with the laws governing the disposition of tax-delinquent land.

(d) Nothing in this section shall prevent any taxpayer from attacking a deed issued by the Commissioner of State Lands on the ground that taxes have actually been paid.

On its face, this statute appears to be a simple cure for tax titles. That is, the former owner must assert his or her rights against the purchaser within a year or be barred forever. There are no cases examining this statute in depth, but there are a number of cases examining a similar, repealed provision codified as Arkansas Statutes Annotated of 1947 § 84-1118 (ASA § 84-1118) which was repealed by Act 626 of 1983. The text of that statute read:

All actions to test the validity of any proceeding in the appraisal, assessment, or levying of taxes upon any land or lot, or part thereof, and all proceeding, whereby is sought to be shown any irregularity of any officer, or defect or neglect thereof, having any duty to perform, under the provisions of this act, in the assessment, appraisal, levying of taxes, or in the sale of lands or lots delinquent for taxes, or proceedings whereby it sought to avoid any sale of lands or lots delinquent for taxes, or proceedings whereby it is sought to avoid any sale under the provisions of this act, or irregularity or neglect of any kind by any officer having any duty of thing to perform under the provisions of this act, shall be commenced within two (2) years from the date of the sale, and not afterward.

The reference to “this act” in the statute was to the provisions regarding proceedings to sell tax forfeited lands. In its simplified form, this statute might read:

All actions...whereby it is sought to avoid any sale under the provisions of this act...shall be commenced within two (2) years from the date of the sale, and not afterward.

This substance of this language is nearly identical to ACA § 26-27-203.⁵⁹ As interpreted by the Court, ASA § 84-1118 did not apply to jurisdictional defects, but only to irregularities.⁶⁰ Irregularities are those defects merely render the tax title voidable and not void. Much of the voidable/void jurisprudence was developed by Arkansas courts examining yet another analogous statute—ACA § 26-38-123 et. seq. (repealed) which provided a 1 year limitations period to challenge a state confirmation of a tax sale. While the Legislature repealed the former ACA § 26-38-123 along with the former ASA § 84-1118, the void/voidable sale jurisprudence remains. Given the similarity in language in the old ASA § 84-1118 and ACA § 26-37-203 plus the court’s standing analysis of a

⁵⁹ Prior to the 2007 amendments of the tax sale statutes, the limitations period in ACA § 26-27-203 was also two years.

⁶⁰ See *Trustees of First Baptist Church v. Ward*, 286 Ark. 238, 691 S.W.2d 151 (1985).

similar statute of limitations (ACA § 26-38-123 et. seq.), it is highly likely that the court’s standing interpretation of ASA § 84-1118 applies to ACA § 26-37-203.⁶¹ This means ACA § 26-37-203 will only cure irregularities and mere defects in the forfeiture process.

Allowing otherwise would give the Legislature the power to breathe life into something that is void, which the Legislature attempts to do in Section (c) of this statute by allowing the COSL to “cure” defects made by county officials, regardless of whether the defect resulted in void or voidable title. Presumably, the language of this section means that if the COSL simply does his duty under the law, the COSL can cure any defect in the tax forfeiture proceeding—whether it renders the deed void or voidable. If this is the intent of the statute, it will likely fail in the courts when faced with a defect that voids the forfeiture.

The Legislature may only cure defects that it had to power to dispense with in the first place.⁶² A taxpayer is afforded Due Process, and whether a given statutory requirement is required by Due Process is up to the courts.⁶³ Thus, where the judiciary determines that a particular requirement vitiates “the power to sell” or is a “jurisdictional defect,” the Legislature is without the power to cure the defect.⁶⁴ Only adverse possession of the property or a binding judicial quiet title will cure a void tax title. The COSL, then, should only have the power to cure defects that void the tax title by performing the mishandled or omitted statutory requirement rather than simply performing only his statutory duties in selling forfeited property. While there is little jurisprudence to support or impugn this position, the prior decisions of the court voiding tax titles when certain defects occur should vest rights in the former owners of property

⁶¹ Footnote 3 of *Riceland Foods, Inc. v. Pearson*, 2009 Ark. 520 is instructive: “The legislature is presumed to know the decisions of the Supreme Court, and it will not be presumed in construing a statute that the legislature intended to require the court to pass again upon a subject where its intent is not expressed in unmistakable language.” (*Citations Omitted*). In *Riceland Foods*, the language regarding the lien statute at issue remained “virtually unchanged” except for some new provisions regarding priority of the lien. On this basis, the court refused to impose a duty on a crop purchaser to inquire if the existence of a lien. See *Riceland Foods*, 2009 Ark. 520 at 10-13.

⁶² See e.g. *Sidway v. Lawson*, 23 S.W. 648, 648-649 (1893) “As to the power of the legislature to cure defects in proceedings, conveyances, and acknowledgments by a retrospective statute, it is said: ‘If the thing wanting or failed to be done, and which constitutes the defect in the proceedings, is something, the necessity for which the legislature might have dispensed with by prior statute, then it is not beyond the power of the legislature to dispense with it by a subsequent statute; and if the irregularity consists in doing some act, or in the mode or manner of doing some act, which the legislature might have made immaterial by prior law, it is equally competent to make the same immaterial by a subsequent law.’” (citations omitted); See also *Carle v. Gehl*, 104 S.W.2d 445, 447-448 (1937) “The Legislature could not dispense with the necessity for the listing and assessing of the property under a valid description or for the levying of the tax upon the property according to its value at a rate not in excess of constitutional limits, or for a sale of the property under proper description by the collector thereunto duly authorized for delinquent and unpaid taxes, or for the sale of the property by the collector under the power. All of these are necessary; to describe the property, ascertain its value by a due assessment, and to fix the legal proportion or rate of the tax and to authorize some designated officer to receive the tax, sell in default of payment, and to convey the property to one who will pay the taxes due thereon.” (Taken from that court’s discussion regarding the Legislature’s ability to cure voiding defects in tax sales by statute).

⁶³ Note 55, *supra*, at 96.

⁶⁴ *Id.* at Footnote 14.

to attack the sale. The Legislature would not have the power to extinguish these vested rights without running afoul of the Constitution.

Another untested provision of this statute is the treatment of negotiated sales. The statute governing negotiated sales allows sale to take place at any time after a failed public sale. Because minerals are not sold at a public sale, the law could treat them as “negotiated sales.” If that is the case, the mineral owner would have only 90 days to discover the sale and file suit to set aside the sale. Mineral sales do not involve any negotiation. The sale is for tax due only. Thus, the sale may not be subject to the abbreviated period for negotiated sales. Any use of the abbreviated period on a mineral tax sale is suspect.

If the abbreviated period were used on a mineral tax title, there is a serious question on the Constitutionality of such a short limitations period. Theoretically, a negotiated sale could take place the day after the public sale. Thus, this taxpayer could lose the right to challenge the sale in only 3 months while another taxpayer who lost their property at the public auction would receive 9 more months to discover the sale and any defects therein.

The final consideration in the effectiveness of the statute of limitation is whether the COSL provided proper notice. In a recent case, the Arkansas Court of Appeals held that the statute of limitations in ACA § 26-37-203 does not begin to run until the COSL actually gives the notice required by statute to the forfeited property owner.⁶⁵

It is very likely that there is no effective statute of limitations or curative statute for mineral tax titles. Because actual possession of minerals is not possible without production, ACA §§ 18-60-212(a) and 18-51-106(a) are highly unlikely to be effective limitations statutes. The weight of authority strongly suggests that ACA § 26-37-203 will be equally ineffective to cure void mineral tax deeds. In the event there is only a voidable defect, ACA § 26-37-203 will likely cure the defect provided that the COSL actually gives notice to the forfeited property owner.

A) Tax Title Defects

Tax forfeitures are both extreme and statutory in nature. Thus, they must be in strict compliance with their organic statutes.⁶⁶ Because government officials must conduct tax forfeitures in strict compliance with statutes, the courts recognize many avenues for property owners to overturn tax sales. This section will review the principles upon which tax sales are overturned.

The case law suggests that there are three possible categories of defects with differing consequences: 1) Irregularities in the execution of the taxation, forfeiture, and sale process (herein, an “irregularity”); 2) Potent defects in the execution of the forfeiture and sale process that go to the State’s jurisdiction to sell the lands (herein, a

⁶⁵ See *Arlands, LLC v. Farmers Bank & Trust Company*, 2009 Ark. App. 747 (2009).

⁶⁶ See *e.g. Lumsden v. Erstine*, 205 Ark. 1004, 172 S.W.2d 409 (1943).

“jurisdictional defect”); 3) Violations of Procedural Due Process. The first two are closely related and will be addressed together, the third will be addressed separately.

Prior to examining these defects, a brief description of the nature of the tax conveyance is necessary.

1. The Nature of a Tax Deed

A tax deed issued by the COSL is a limited warranty deed.⁶⁷ It is distinguishable from a tax redemption deed, which creates no title.⁶⁸ This is very important to remember when examining titles because many holders of void interests who let their “interests” lapse for unpaid taxes often redeem those void interests when there is an active oil or gas play. Some of these redemptions occurred after the statute change in 1985 which cut off the defense of failure to subjoin. That fact is irrelevant because the act of redemption only affects the former title and does not create any new title. Because the tax deed is a limited warranty deed, it offers no assurance from the state as to the marketability of the title. A tax deed passes the title of former owner along with any future interests, whether in the former owner (e.g. reversions) or in another (e.g. remainder interest).⁶⁹ In no event, however, does a tax title pass any title not in the scope of the mineral severance or reservation.⁷⁰

2. Irregularities v. Jurisdictional Defects

Whether a defect is an “irregularity” or jurisdictional defect that “goes to the power to sell” is a judicial determination.⁷¹ The “power to sell” refers to the jurisdiction of acting state official to take and convey the title of a taxpayer.⁷² An “irregularity” is anything that does not go to the power to sell. To have the power to sell, the taxing authority must have the concurrent existence of all of the following:⁷³

1. A valid law;
2. A lawful tax;
3. Legally assessed;
4. Legally levied;
5. On land liable for tax;
6. With the owner fairly in default.

⁶⁷ ACA § 26-37-302.

⁶⁸ *Chavis v. Taylor & Co.*, 211 Ark. 252, 254-255, 200 S.W.2d 507, 508 (1947) (“The effect of a redemption from the state of land forfeited for delinquent taxes is not to vest in the person making redemption the title which the state obtained by virtue of the delinquent tax sale, but merely to extinguish any right or lien of the state growing out of the said delinquent tax sale proceedings.”).

⁶⁹ *See Edwards v. Hall*, 267 Ark. App. 1003, 593 S.W.2d 465 (1983).

⁷⁰ *See Brizzolara v. Powell*, 214 Ark. 870, 218 S.W.2d 728 (1949).

⁷¹ *See* ACA § 26-37-302.

⁷² *Id.* at 1005, 411.

⁷³ *Id.*

The consequences of having a mere irregularity versus a jurisdictional defect are significant. Arkansas Code § 26-37-203 should amount to an absolute defense to mere irregularities after one year past the issuance of the tax deed while a jurisdictional defect can only be cured by actual possession of the minerals. Thus, when one encounters a jurisdictional defect in a mineral tax deed, it is very likely that the mineral tax deed is void and can be set aside.

It is not possible to determine when a defect is jurisdictional without some existing judicial guidance. Presently, there are several common defects recognized by Arkansas courts as vitiating the power to sell:

1. Unlawful assessment
2. Void legal descriptions.
3. A void tax upon the land.
4. Taxes levied on land exempt from taxation.
5. Excessive expenses or charges.
6. Taxes already paid or no tax due.

These are general classes of cases and do not represent every possibility. Each is treated in depth below.

i) Unlawful Assessment

For those new to oil and gas title in Arkansas, it may be a surprise that prior to 1985, there is no possibility of a valid mineral tax deed without judicial intervention. This originated from a 1950 ruling of the Arkansas Supreme Court. In *Sorkin v. Myers*,⁷⁴ the Court ruled that the Ouachita county assessor's failure to list and subjoin severed mineral interests in the same assessment book as all other interests in the property constituted fatal defect in the tax sale procedure that went to the power of the state to sell the property for forfeited taxes. The duty to subjoin was not express by statute, but the court implied this duty from legislation regarding timber rights, which the court likened to mineral rights.⁷⁵ Subsequent suits demonstrated that Columbia,⁷⁶ Union,⁷⁷ Miller,⁷⁸ Franklin,⁷⁹ Johnson,⁸⁰ and Pike⁸¹ county assessors committed the same or similar misfeasance in listing and subjoining severed mineral interests to the remainder of the real property interests in the assessment book. Others report lack of listing or joinder in assessment books as a defect in every county in Arkansas—including the counties lying

⁷⁴ 216 Ark. 908, 227 S.W.2d 958 (1950).

⁷⁵ *Sorkin*, 216 Ark. 911-12, 227 S.W.2d 960.

⁷⁶ *Davis v. Stonecipher*, 218 Ark. 962, 239 S.W.2d 756 (1951).

⁷⁷ *Stienbarger v. Keever*, 219 Ark. 411, 242 S.W.2d 713 (1951).

⁷⁸ *Smiley v. Thomas*, 220 Ark. 116, 246 S.W.2d 419 (1952).

⁷⁹ *Adams v. Bruder*, 275 Ark. 19, 627 S.W.2d 12 (1982).

⁸⁰ *Blackburn v. Cline*, 8 Ark. App. 209, 650 S.W.2d 588 (1983).

⁸¹ *Garvan v. Potlatch Corp.*, 278 Ark. 414, 645 S.W.2d 957 (1983).

in the Fayetteville Shale.⁸² December 2009 saw the first reported case regarding unlawful assessment in a Fayetteville Shale County.⁸³

In short, a tax deed for a severed mineral interest issued for taxes due prior to April 15, 1985, without a valid judicial intervention is no good. Without actual possession of the minerals or a binding quiet title, a pre-1985 tax title has no possibility of validity. After 35 years, the Legislature finally addressed *Sorkin* by enacting Act 961 of 1985, which expressly allowed the assessor to list mineral interests separately from other real property interests. The defense of unlawful assessment has no direct applicability to newly forfeited mineral interests, but may be an indirect defense as when a void forfeiture becomes re-forfeited.

ii) Defective Legal Descriptions

A defective legal description in the assessment or tax deed renders the tax forfeiture void.⁸⁴ An acceptable legal description “should be such as will be readily understood by persons even ordinarily versed in such matters” while a void description is “a description which is intelligible only to persons possessing more than average intelligence” or couched in such a terms that “the use and understanding of which is confined to the locality in which the land lies.”⁸⁵ Also, the description itself—without consulting extrinsic sources—must furnish a key to identifying the property.⁸⁶

The courts reviewed this standard many times, and there are a number of possible defects in a legal description that can void an assessment and/or a tax deed. A legal description using “part of” without further calls that identify the property does not meet this standard.⁸⁷ For example, “Part of the Southeast Quarter” is insufficient while “Part of the Southeast Quarter described as beginning at the Southwest corner, thence North 100 yards, East 100 yards, South 100 yards, and West 100 yards to the beginning” is valid. In general, a lot and block description is sufficient provided that there are no confounding factors such as a duplicate block or no subdivision identified.⁸⁸ Metes and bounds descriptions are acceptable if the descriptions are correct.⁸⁹ For a metes and

⁸² See e.g. Thomas A. Daily and W. Christopher Barrier, WELL, NOW, AIN'T THAT JUST FUGACIOUS!: A BASIC PRIMER ON ARKANSAS OIL AND GAS LAW, 29 U. Ark. Little Rock L. Rev. 211, 220 (2007). (“[T]he authors have concluded that, at least prior to 1986, there was never a single, valid assessment of a severed mineral interest in the State of Arkansas.”).

⁸³ See *Selrahc LP v. SEECO, Inc.*, 2009 Ark. App. 865 (2009).

⁸⁴ See *Shelton v. Byron*, 206 Ark 665, 177 S.W.2d 421 (1944).

⁸⁵ *Toler v. Fischer*, 201 Ark. 1107, 148 S.W.2d 159 (1941).

⁸⁶ *Lemon v. Tanner*, 173 Ark. 414, 292 S.W. 668 (1927). (“The rule is that a description of land is sufficient if the land can be located by evidence aliunde from the description itself. If the descriptive words themselves furnish a key for identifying the land conveyed, nothing more is required.”)

⁸⁷ See generally: *Graysonia-Nashville Lumber Co. v. Wright*, 117 Ark. 151, 175 S.W. 405 (1915); *Arkansas Trust Co. v. Sims*, 198 Ark. 1143, 133 S.W.2d 854 (1939); *Price v. Price*, 207 Ark. 804, 182 S.W.2d 879 (1944); *Van Meter v. Addington*, 250 Ark. 598, 466 S.W.2d 249 (1971).

⁸⁸ See e.g. *Dodson v. Thomason*, 217 Ark 281, 233 S.W.2d 395 (1950) (tax deed description void because it identified property as being on Block B when there were many block B's in the city) ; *Massey v. Bickford*, 208 Ark. 685, 187 S.W.2d 541 (1945) (description giving wrong subdivision ruled void).

⁸⁹ See e.g. *Alphin v. Banks*, 193 Ark. 563, 102 S.W.2d 558 (1937).

bound description, a definite point of beginning and closure are essential.⁹⁰ The use of “fractional” is acceptable so long as it refers to a government subdivision and is not a “fractional part of” which fails to further identify the tract by metes and bounds.⁹¹

iii) Void Taxes

The subject of illegal taxes could take many pages of material to offer a modest introduction. When seeking to determine the validity of a tax sale for illegal taxes, a title examiner should engage the services of an attorney familiar with illegal taxation. Notwithstanding the breadth and depth of this area of the law, there are some less arcane taxation issues that are easy for non-experts to master.

A levy beyond the legal rate is easy to determine. One should examine the tax ordinances in effect at the time of the forfeiture, then compare the ordinances to both the tax levy and the Constitutional limits. If the levy is greater than enacted rate, the forfeiture is void.⁹² If the enacted rate is greater than the Constitutional limit, the forfeiture is void.⁹³ Every property tax other than city general funds, county general funds, and county road funds must be approved by voters under the jurisdiction of the taxing entity.⁹⁴ Thus, a property tax levied and extended without an election will void a tax sale. An irregularity in the proceedings to create or levy an otherwise lawful tax (not beyond Constitutional limit or purpose) does not void the tax. For example, an irregularity in the vote for the tax or levy thereof does not create a void tax.⁹⁵ Any property tax levied for a particular purpose can only continue so long as the purpose exists.⁹⁶ Property taxes must also not be based on no more than 20% of the property’s value.⁹⁷ It is worthwhile to determine what, if any, market value the assessor placed on a mineral interest. The right to appeal the assessor’s valuation ends long after the forfeiture, but a complete absence of a market value could result in a void tax.

Obviously, taxation beyond the local government entity’s authority results in a void tax. That is, a government entity cannot extend taxes beyond its incorporated geographical area.⁹⁸

⁹⁰ See *Mode v. Henley*, 227 Ark. 875, 302 S.W.2d 73(1957) (lack of definite point of beginning renders deed void); *Undernehr v. Sandlin*, 35 Ark.App. 207, 827 S.W.2d 164 (1992) (description failed to return to point of beginning).

⁹¹ See *Graysonia-Nashville Lumber Co. v. Wright*, 117 Ark. 151, 175 S.W. 405 (1915).

⁹² For example, there is a reported case where the Franklin County Quorum Court levied a fifteen hundredths mills tax for fire-fighting equipment, but the tax rate in effect at the time was fourteen hundredths mills *Cohn v. Little*, 199 F.2d 28 (E.D. Ark. 1952).

⁹³ See Arkansas Constitution Art. 16 § 9, Art. 12 § 4, Amend. 62, Amend 74, Amend. 31, Amend. 37, and Amend. 32.

⁹⁴ See *Fuller v. Wilkerson*, 198 Ark. 102, 128 S.W.2d 251 (1939).

⁹⁵ See *Ingram v. Blackmon*, 202 Ark. 769, 152 S.W.2d 315 (1941).

⁹⁶ See *Daniel v. Jones* 332 Ark. 489, 966 S.W.2d 226 (1998); Ark. Const. Art. 16 § 11.

⁹⁷ ACA § 26-26-303.

⁹⁸ See e.g. *Frizzel v. Lowe*, 174 Ark. 287, 294 S.W. 996 (1927) (sale of land forfeited for Clark County taxes where land was in Ouachita County held void).

Errors in the calculation of the tax also fall under the aegis of void or illegal taxes. That is, the clerk or assessor made a miscalculation of the tax due by using the wrong rate or the wrong property value, or there was a malfunction in the computing process. In *Walsh v. Keazy*,⁹⁹ a computing error by a mechanical calculator caused the tax due to appear 2 cents over the actual amount due. This mere 2 cent overage voided the entire sale.

Again, this is only a small window into the possibilities for illegal taxes, and you should consult an attorney experienced in illegal exactions if it becomes necessary to use this defect as a defense against a tax deed.

iv) Exempt Lands

This facet presents few applicable defenses in severed mineral tax titles because most exempt lands are public lands. There are some instances, however, where this defect can apply to private lands. The court held in *Ponder v. Richardson*¹⁰⁰ that a private tract with a non-profit public cemetery was overtaxed where the assessor included the acreage of the cemetery in the value of the property. The author notes that this really doesn't make the rest of the private tract exempt, but instead, the included tax exempt property became a "poison pill" that caused the private tract to have greater tax due than necessary. This fails the "illegal assessment" prong of the power to sell.

Another instance where this could apply is where the lands taxed are used for some public purpose, such as a community school, but the land is under a reversion clause that will place the land back into private ownership upon the abandonment of the public use.¹⁰¹

These situations don't readily apply in a severed mineral context. Because a mineral severance is a separate estate that can be assessed separately from a surface interest, a tax deed for minerals under lands used for a public purpose would probably not be void simply because there is some exemption on the surface estate, though it may be an open question as to whether the mineral interest of a charity organization is exempt from ad valorem taxation.

v) Excessive or Unauthorized charges

Act 626 of 1983 removed the county from process of selling tax forfeited lands. Thus, the old statutes authorizing certain charges for issuing deeds and processing forfeitures by the counties removed a large source of excessive and unauthorized charges.

⁹⁹ 224 Ark. 773, 276 S.W.2d 71 (1955). This court stated: "A tax overcharge is not legal. When once it is conceded that the sale was for an excess of as much as 1¢, then the power to sell has been destroyed. Just as the sovereign would be justified in refusing to accept from the citizen one cent less than the correct tax, so the citizen is justified in saying that the 'power to sell' has been destroyed when the sovereign sells the property for 1¢ more than the correct tax. Mechanical devices are fine; but the sovereign cannot use them to overcharge a citizen in his taxes."

¹⁰⁰ 213 Ark. 238, 210 S.W.2d 316 (1948).

¹⁰¹ See e.g. *Leavy v. Wood*, 208 Ark. 235, 185 S.W.2d 708 (1945).

This change should leave little room for error by the COSL who now controls the sale process, but there are a number of fees remaining in the statutes which could provide fertile ground in future litigation.

The law allows \$1.50 per tract per publication insertion for notices required by statute at both the county and state level.¹⁰² The law also allows the COSL a \$5 fee for the redemption deed¹⁰³ and all recording fees as set by statute.¹⁰⁴ Also, the law authorizes the COSL to apply a 10% delinquency penalty per year and 10% interest per year.¹⁰⁵ Finally, the COSL can charge for “costs” incurred by the County and the COSL.¹⁰⁶ Authorized costs include: certified mail costs, newspaper and catalog costs, and title work.¹⁰⁷ If it can be shown that any of the “costs” levied by the COSL are unnecessary or excessive, there is room to litigate because of the strong precedent that indicates that even the slightest overcharge would void the sale:¹⁰⁸

If the excess is as much as one cent, then the Power to Sell is vitiated. In the case at bar it was stipulated that the excess was five cents. If a citizen's property can be taken from him by the sovereign for an excess of five cents, then by the same token it can be taken from him for an excess of five million dollars. If a citizen's rights and property are to be safe, then they must be kept safe against little exactions as well as against large encroachments. The constant drip of water will wear away the largest stone; and if the sovereign by constant inroads in small things is allowed to take the citizen's property, then the rights of private ownership are gone to the realm of Limbo. Courts are to protect the rights of citizens--that is one of the reasons for the existence of judicial tribunals.

There has not been a “costs” case since the COSL took over the tax sale process in 1983. It is evident that this violation of the power to sell still has life left in it. The author can imagine a scenario where the COSL overreaches in billing out the “title work” done in relation to a tax sale.

vi) Taxes were already paid

This requires little explanation. The statutes provide that the sales of land for which there is no tax due are void.¹⁰⁹ A valuable extension of this is that when taxpayer attempts to pay taxes due, a mistake or oversight on the part of the collector renders the sale void.¹¹⁰ This manifests itself commonly in the collector refusing to take payment of taxes for mineral interests. When dealing with this situation, it is best to obtain written evidence of the refusal for future use. Collectors that refuse taxes on severed minerals often include a letter explaining that the county does not assess minerals. This is sufficient to defend against a later forfeiture.

¹⁰² ACA §§ 26-37-107 and 26-37-201.

¹⁰³ *Id.*

¹⁰⁴ ACA § 26-37-303.

¹⁰⁵ *Id.*

¹⁰⁶ *Id.*

¹⁰⁷ ACA § 26-37-104.

¹⁰⁸ *Lumsden v. Erstine*, 205 Ark. 1004, 172 S.W.2d 409 (1943).

¹⁰⁹ ACA § 26-37-206.

¹¹⁰ *Brown v. Bridges*, 227 Ark. 1006, 304 S.W.2d 939 (1957).

3) Due Process

Perhaps the least understood aspect of tax deeds is Due Process, the right of which is guaranteed under the 14th Amendment of the U.S. Constitution. There are two varieties of Due Process: Substantive and Procedural. With tax sales, Procedural Due Process (PDP) is the most applicable. PDP requires, at a minimum, notice and an opportunity to be heard when a party faces the loss of life, liberty, or property. The most vexing issue in Arkansas tax sales now is the notice prong of PDP.

Notice sufficient to satisfy Due Process must be more than a mere gesture. It must be reasonably calculated to inform parties facing the deprivation of a property interest of the right to defend. That is, considering the character of the proceedings, the actions taken to give notice must be done “as one desirous of actually informing the absentee might reasonably adopt.”¹¹¹ This is an elusive standard.

In past disputes over the notice requirement in Arkansas’s tax forfeiture proceedings, Arkansas courts refused to look beyond the requirements of the statute when determining whether a tax sale could be overturned for lack of notice.¹¹² When first challenged on Constitutional Grounds, the Arkansas Supreme Court ruled that the procedure in place—which only required publication of notice prior to the sale and a notice by certified mail prior to the sale—was sufficient even when the COSL received the certified mail back as “unclaimed” and “forwarding order expired.”¹¹³ The Arkansas Supreme Court required nothing further of the COSL than compliance with the statute.

Reasonable minds might differ as to whether this was correct. Arkansas places an affirmative duty on those owning real property to furnish a list of that real property to the collector.¹¹⁴ Thus, the state has a defensible argument that any lack of notice was brought on by the negligence of the property owner. Then again, the United States Supreme Court said in prior cases that reviewing courts must consider:

“[T]he private interest that will be affected by the official action; second, the risk of an erroneous deprivation of such interest through the procedures used, and the probative value, if any, of additional or substitute procedural safeguards; and finally, the Government’s interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirement would entail.”¹¹⁵

The flaw in Arkansas’s first review of the notice statute for Constitutionality was that the Arkansas court didn’t go far enough in its analysis of what additional procedures

¹¹¹ Mullane v. Central Hanover Bank & Trust Company, 339 U.S. at 312 (1950).

¹¹² See Jenny Wilkes Robertson, Note, FOURTEENTH AMENDMENT DUE PROCESS CLAUSE AND NOTICE TO BE HEARD—IT FELT SO RIGHT BUT WAS ALL SO WRONG: UNITED STATES SUPREME COURT RULES ARKANSAS’S TAX-FORECLOSURE NOTICE PROCEDURE FAILS TO SATISFY DUE PROCESS CLAUSE WHEN CERTIFIED MAIL NOTICE RETURNS “UNCLAIMED.” Jones v. Flowers, 126 S. Ct. 1708, (2006), 30 U. Ark. Little Rock L. Rev. 198-99 (2007).

¹¹³ See *Id.* at 200-201.

¹¹⁴ ACA §26-26-501.

¹¹⁵ Mathews v. Eldridge, 424 U.S. 319 (1976).

could safeguard a property owner's interest and what burdens those additional procedures might entail. The requirement for this sort of examination leaves open indefinitely the question of whether a particular set of facts under a statute is in compliance with Due Process. Had the Arkansas Court addressed this aspect of Due Process analysis, *Jones* may never have happened.

On July 28, 2003, the saga of *Jones v. Flowers* began. It culminated with no less than a review by the United States Supreme Court. The facts of *Jones* closely paralleled Arkansas's first Constitutional review of the notice statute.¹¹⁶ That is, the certified mail notice required by statute came back marked "unclaimed."¹¹⁷ The Supreme Court ruled that the certified letter was not enough notice, but offered no serious alternatives for the State to follow.¹¹⁸

In response to the case, the Legislature modified ACA § 26-37-301 to include a follow up notice by regular mail when the certified letter is not claimed and ACA § 26-37-202 to include a follow up notice to the owner by regular mail after the sale. The Legislature, however, did not amend ACA § 26-37-201 to comport with the *Jones* decision. This means the statute is prima facie Unconstitutional unless there are some grounds for distinguishing the notice requirements for surface and mineral interests.

Yet another problem with the mineral tax deed notice statute is that it affords no protection to interested parties who are not the "record owner." The regular notice provisions for fee and surface estates include provisions that all "interested persons," being those with an interest of record, receive notice. As such, Arkansas's notice statute for mineral tax interests fails Constitutional muster under the ruling of *Mennonite Bd. of Missions v. Adams*.¹¹⁹ It is easy to imagine a scenario where the owner of an oil and gas lease that is inferior to a tax lien could fail to receive notice of the forfeiture of the mineral interest upon which his lease is based.

The effect of *Jones* and *Mennonite Board of Missions* on mineral tax deeds is unclear. Because there is probably no effective statute of limitations and no adverse possession for tax deed minerals, a claim that the notice statutes are Unconstitutional is probably not a moot claim. Without actual production of the minerals, there is no appreciable argument to apply laches or estoppel to a claim by the former owner of the interest. ACA § 26-37-203 probably would not cure or limit the ability of one to bring a suit under *Jones* or *Mennonite Board of Missions*. Recall that the last requirement for the state to obtain jurisdiction to sell tax forfeited property is that the "owner be fairly in default." If the notice given to the mineral owner is not Constitutionally sufficient, how could the State satisfy this burden? If this is the case, it is possible that these rulings made all mineral tax titles void with no hope of curing save for actual production.

¹¹⁶ See Robertson, *supra*, note 112 at 202-207.

¹¹⁷ *Id.*

¹¹⁸ See Robertson, *supra*, note 112 at 211-14.

¹¹⁹ 462 U.S. 791 (1983).

IV. Reform: A Modest Proposal

Arkansas should explore other options for funding local governments by taxing minerals. To replace the ad valorem tax on minerals with another type of tax, such as an increase in the severance tax, a gross production tax, or a net production tax—with turnbacks to local governments—would require a Constitutional Amendment. Because this is an arcane and difficult issue, replacing ad valorem taxation of minerals by Amending the Constitution would face considerable obstacles with voters. Most likely, ad valorem taxation of minerals in Arkansas will remain a part of Arkansas law for the foreseeable future.

In the absence of a Constitutional Amendment, effective Legislative reform is possible. Past Legislative reform on tax deeds, both mineral and fee, was reactionary to court decisions. Those court decisions were doubtlessly based on some idea of fairness to taxpayers. The harsh remedy of enforcement compels courts over time to wear gaping holes in the state's power of enforcement for delinquent property taxes. This is most evident in mineral tax deeds. As a result, local school districts, libraries, hospitals, and police departments miss out on needed revenue because there is little incentive for taxpayer compliance. The key to Legislative reform, then, should be to reform the enforcement process for delinquent ad valorem taxes on minerals. Reform can take place in with two simple steps:

1. Exempt minerals from forfeiture to the state.

The forfeiture remedy is the reason why courts are so harsh in their interpretation of the statutes.

2. Make ACA § 26-36-212 the exclusive remedy of local taxing units for unpaid ad valorem taxes on mineral interests.

The text of ACA § 26-36-212 is as follows:

Oil or gas interests

(a)(1) When the ad valorem taxes on working interests, royalty interests, or overriding royalty interests in oil or gas of any taxpayer is delinquent for a period of one hundred eighty (180) days or more, any one (1) or more taxing units which are entitled to a portion of the delinquent taxes when collected shall have a cause of action against the delinquent taxpayer for that portion of the delinquent taxes and costs of collection, including the penalty and interest thereon, to which the taxing units are entitled, plus a reasonable attorney's fee.

(2)(A) Any such action shall be brought in the chancery court of the county in which the delinquent taxpayer resides or in which property of the delinquent taxpayer is situated.

(B) Any judgment awarded a taxing unit in such cause of action shall be enforceable to the same extent and in the same manner as other civil judgments.

(b)(1) Any taxpayer offering to redeem tax-delinquent property after an action has been filed as authorized in this section shall be required to pay costs, including attorney fees, incurred by any taxing unit in pursuing its remedies under this section.

(2) When any judgment rendered against a delinquent taxpayer pursuant to this section is satisfied, the tax liability on the property and the amount required to be paid to redeem the property shall be reduced by the amount of the taxes, penalty, and interest included in the judgment.

This statute, with some modification, could become an easy solution to the problem of uncollected taxes and unmarketability of mineral tax titles. The obvious advantage is that it is a judicial procedure subject to all of the Arkansas Rules of Civil Procedure. This eliminates notice problems under *Jones* and *Mennonite Board of Missions*. It also provides the binding effect of *Res Judicata*. The taxpayer would have to raise arguments against the validity of the tax in the judicial proceeding or waive those arguments. The grounds to set aside a judgment are far more limited than to set aside a tax deed. Finally, a judgment rendered under this statute is against the taxpayer personally. This means there is no transfer of title, but there is a judgment lien on the property. The taxing unit could then satisfy the lien by executing on the judgment debtor's property.

Only if it were necessary to execute on the mineral interest itself would the title transfer to another party. This happens at an execution sale. The execution sale has the benefit of judicial safeguards, including the public sale for a reasonable bid. The purchaser of the interest at any execution sale would gain the advantage of a powerful 5-year statute of repose for lands purchased at judicial sales.¹²⁰ The party losing title at the sale would have the added advantage of the excess proceeds going into the registry of the court, which would not be subject to the harsh restrictions of the COSL's land proceeds fund. The excess proceeds would eventually escheat to the State Auditor where they would be subject to the Great Arkansas Treasure Hunt. All of this could happen without costing the taxing unit any money because the statute provides for a reasonable attorney's fee and costs.

A final advantage to the taxing unit would be to return the interests to the tax rolls sooner. While forfeited to the state, the taxing receives no revenue from the interest. This statute provides that six months after October 10, year 2, that unit may sue to collect the taxes. The tax forfeiture statutes force the county to hold the interest for a year, then the COSL for one year before there is any chance of the interest returning to the tax rolls. A skilled lawyer can reduce a one-sided collection case to a judgment in a matter of a month or two. The execution and sale process would take another month or two. At the most, the entire judicial foreclosure process would take perhaps 6 months. This is a full year before the COSL could sell the interest, providing that the surface owner even bothered to apply to purchase the interest under his/her exclusive option to purchase. A workable version of the statute might be:

¹²⁰ ACA § 18-61-105.

Oil or gas interests

(a)(1) When the ad valorem taxes on working interests, royalty interests, or overriding royalty interests in oil or gas of any taxpayer is delinquent for a period of one hundred eighty (180) days or more, any one (1) or more taxing units which are entitled to a portion of the delinquent taxes when collected in which the interest lies shall have a civil cause of action against the delinquent taxpayer for that portion of the delinquent taxes and costs of collection, including the penalty and interest thereon, to which the taxing units are entitled, plus a reasonable attorney's fee.

(2)(A) Any such action shall be brought in the chancery circuit court of the county in which the delinquent taxpayer resides or in which property of the delinquent taxpayer is situated.

(B) Any judgment awarded a taxing unit in such cause of action shall be enforceable to the same extent and in the same manner as other civil judgments.

~~**(b)(1) Any taxpayer offering to redeem tax delinquent property after an action has been filed as authorized in this section shall be required to pay costs, including attorney fees, incurred by any taxing unit in pursuing its remedies under this section.**~~

~~**(2) When any judgment rendered against a delinquent taxpayer pursuant to this section is satisfied, the tax liability on the property and the amount required to be paid to redeem the property shall be reduced by the amount of the taxes, penalty, and interest included in the judgment.**~~

These changes eliminate references to the COSL forfeiture process and the reference to chancery court. In addition to this change, the Legislature would need to repeal or modify many other statutes, particularly those in Title 26 pertaining to the forfeiture and sale of tax delinquent property.

V. Conclusion

Arkansas faces many challenges in taxing severed mineral interests. Because non-producing minerals are no longer valued for assessment, the largest source of past void mineral tax titles, is no more. As county Assessors in the Fayetteville Shale become more comfortable assessing and valuing producing mineral interests, a new tide of mineral forfeitures will flow. This will generate more litigation and inevitably, more legislation.

Title examiners should remain skeptical of all mineral tax deeds. To date, there is no absolute cure for defective mineral tax titles, save for actual possession and production of the minerals. Defects are numerous, and many are outside of the county real estate records. The Constitutional shortcomings of the mineral tax sale notice statute are also a source of serious risk of title failure.

The author proposes that taking mineral interests out of the legislative forfeiture process is the best means to achieving marketable title for forfeited tax mineral interests. A judicial enforcement mechanism would simplify the enforcement process with no cost to the local taxing units and speed the return of the delinquent minerals to the tax rolls with a greater chance of obtaining marketable title.

Appendix A

2006 Assessment Coordination Department Rules for Valuation of Minerals

STANDARD FOR ASSESSING MINERAL RIGHTS

TERMINOLOGY AND DEFINITIONS

Mineral rights, without regard to the surface rights or usage, and when not in actual development or contiguous to one, have a potential value only. Depending on the location and type of deposit, the value present usually reflects the present worth of the ultimate recovery at some future date using a capitalization rate that takes into account the risk involved. Simply stated, the present value of mineral rights is the gross value of future production, less all expenses necessary for production and allowances for depletion.

In Arkansas, there are four general classifications of mineral ownership. Each of these types are to be handled differently, and are discussed on the following pages.

1. **Mineral Leases - Non-Producing or Exploratory.** As stated in the Attorney General's Opinion number 85-133 dated June 17, 1985, these are considered exempt from ad valorem taxation.
2. **Severed Mineral Rights.** These are defined as mineral rights that are separated from the surface rights by deed. Severed mineral rights are to be assessed in the Real Estate Assessment Book on the line following the surface rights and designated as Mineral Rights Only. As an option, you may make a separate Mineral Assessment Book in the same order of legal description as the Real Estate Book.
3. **Mineral Rights Retained With the Surface Rights - No Separating Deed Issued.** For non-producing minerals, there is no separate listing. Only the surface rights are listed in the Real Estate Assessment Book. Where there is a known and proven mineral value, but no production, you may include the value with the surface value.
4. **Producing Mineral Rights.** When minerals are in active production, assessments and billings become more complicated, and must be made with care. A clear understanding of various terms and valuation procedures is important, and are defined on the following pages.
 - 4.1 **Operator/Producer.** These two terms are used interchangeably, and refer to the individual or company that is responsible for the lease operations and production. Most of the time (although not always), the Operator/Producer is owner of the Working Interest in the mineral operation.
 - 4.2 **Transporter.** This is the purchaser of the mineral being produced. Depending on the type of mineral, the Transporter can be a pipeline company, rail company, barge company, truck line, tank farm or refinery. Ownership of the mineral passes to the Transporter at the sales meter or scales.

4.3 Division Order. A Division Order, as the name implies, describes how the proceeds of the production are to be divided among the various interests. Total interests must be equal, but cannot exceed 100%. In a new lease the Operator/Producer will have the original Division Order. As changes occur in the various interests, the changes are kept track of by the Transporter and they will have the most current copy. When in doubt, check with the Operator first, and they will direct you to the proper location of the current Division Order.

Since each owner must be assessed, a new Division Order should be obtained each assessment year. The Division Order will give a list of the individual owners and their percentage of participation which is needed to make the current assessment.

In the case of the Working Interest, assessments are made in the name of, and taxes billed to the Operator/Producer. With Royalty and Overriding Interests, assessments are made, and taxes billed to each individual owner.

There are three general types of interest ownership:

4.3.1 Working Interest. The Working Interest is the person or company who owns the right (lease) to extract the mineral. The Working Interest participation is usually 87.5% (.875), although this can vary depending on any Overriding Interest as defined in 4.3.3.

4.3.2 Royalty Interest. The Royalty Interest owner(s) is the person or group of persons who own the mineral rights to the minerals being produced. Total Royalty Interest is usually 12.5% (.125) of the production value. There can be many Royalty Interest owners, each with a percent of the total Royalty Interest. Each Royalty owner's share is shown on the Division Order.

4.3.3 Overriding Interest. An Overriding Interest is similar to a Royalty Interest in that the Overriding Interest owner assumes none of the risk of the Producer. The Overriding Interest can be part of the Working Interests' 87.5% (thus reducing the Working Interest), or part of the Royalty Interests' 12.5% (reducing the total Royalty Interest). Any Overriding Interest will also be spelled out in the Division Order.

MINING.....LAND

Among the raw materials produced in Arkansas by mining and quarrying are the following: abrasives, agricultural limestone, barite, bauxite, chalk, clay, coal, crushed stone (trap rock), dolomite, fuller's earth, gem stones, gravel, gypsum, industrial sand, lead, lightweight aggregates, limestone (crushed and dimension), manganese, molybdenum, nephelinite syenite, novaculite, phosphate, rock, refractories, roofing granules (from granite deposits), sand and gravel, shale, slag, slate, stone (crushed and dimension), talc, vermiculite and zinc.

Method

The method for arriving at the value for purposes of assessment, insofar as it is applicable to land owned in fee simple (including all mineral rights), by the operating company, should be as follows:

1. The land according to its capability classification.
2. All improvements and fixed appurtenances on the land, such as buildings, roads, and all other improvements of a permanent character.
3. The mineral deposit as it is rendered by the owner and or operating company when the amount rendered is in conformity with the Assessor's evaluation.

The total of the three items above constitutes the Real Property assessment of the owner's and/or the operating company's land and mineral deposit, insofar as it applies to an active mineral deposit.

An inactive mineral deposit **should not** be assessed except in certain instances, such as proven areas, etc.

MINING.....ROYALTY

Where there is a royalty interest in a mining property such as limestone, coal, bauxite, barite, etc., the method for arriving at the market value for purposes of assessment is as follows:

- 1. Limestone.** Estimated value (according to Arkansas Geological Commission) is \$6.00 per ton X 12.5% (going royalty rate) = \$.75 gross royalty per ton (Assessment Coordination Division recommends using a range of \$.50 to \$1.00). Deduct the necessary expenses, if any, and the sum remaining is the net royalty. Net royalty X 20% = the Assessment.
- 2. Coal - Stripping Operation.** Estimated value (according to Arkansas Geological Commission) is \$40.00 per ton X 12.5% (going royalty rate) = \$5.00 gross royalty per ton (Assessment Coordination Division recommends using a range of \$4.00 to \$5.00). Deduct the necessary expenses, if any, and the sum remaining is the net royalty. Net royalty X 20% = the Assessment.
- 3. Bauxite.** Estimated value (according to Arkansas Geological Commission) is \$15.75 per ton X 12.5% (going royalty rate) = \$1.96 gross royalty per ton (Assessment Coordination Division recommends using a range of \$1.00 to \$2.00). Deduct the necessary expenses, if any, and the sum remaining is the net royalty. Net royalty X 20% = the Assessment.
- 4. Barite.** Estimated value (according to Arkansas Geological Commission) is \$22.50 per ton X 12.5% (going royalty rate) = \$2.81 gross royalty per ton (Assessment Coordination Division recommends using a range of \$2.00 to \$3.00). Deduct the necessary expenses, if any, and the sum remaining is the net royalty. Net royalty X 20% = the Assessment.
- 5. Bromine Brine.** Estimated value (according to Arkansas Geological Commission) is \$.30 per bbl. (Assessment Coordination Division recommends using a range of \$.03 to \$.05). Deduct the necessary expenses, if any, and the sum remaining is the net royalty. Net royalty X 20% = the Assessment.

ASSESSMENT TABLES FOR PRODUCING GAS WELLS

Formulas and Minimum Pricing Guidelines

\$6.19 per M.C.F. X 365 days= \$2259 Annual Value per M.C.F.

WORKING INTEREST

Formula to arrive at assessed value:

Price X Working Interest percent % - Production Expenses (13%) X .20 Assessment Rate =
Assessment Value per M.C.F. Average Daily Production (A.D.P.)

Example:

$\$2259 \times .875 = \$1977 - .13 = \$1720 \times .20 = \344.00 Assessed Value per M.C.F. A.D.P.

ROYALTY INTEREST

Formula to arrive at assessed value:

Price X Royalty Interest percent % X .20 Assessment Rate =
Assessed Value per M.C.F. Average Daily Production (A.D.P.)

Example:

$\$2259 \times .125 = \$282 \times .20 = \$56.00$ Assessed Value per M.C.F. A.D.P.

The above prices reflect current averages. If contract pricing is higher or lower than \$2259 per M.C.F., then you should use the contract price. Request a copy of the contract for your files for verification and documentation of using a different price.

Rounding in the above examples is to the nearest whole dollar for simplicity. In application, you may round to the nearest whole penny. Whichever rounding method you use, use it for all mineral assessments.

Note: A Division Order must be provided for each oil and gas lease or unit so individual interests can be assessed correctly. If no Division Order is provided, the total 8/8 value shall be assessed to the operator.

ASSESSMENT TABLES FOR PRODUCING OIL WELLS

The Assessment Tables are computed from the following:

1. Average price of oil on the Arkansas Market.
2. Price adjusted for severance tax and property (real estate) tax.
3. Assumptions.
 - a. Price of oil per barrel - \$36.12
 - b. Decline rate - 30% per year - 20% on stripper
 - c. Discount factor - 15.0%

Per Well Production Class (bbls per day)	Working Interest Assmt. Amount X % of Interest	Royalties & Overrides Assmt. Amount X % of Interest
0 - 2	1274	1967
2.1 - 5	2555	5410
5.1 - 10	4046	6217
10.1 - 25	3834	5072
25.1 - 50	3819	4658
50.1 - 70	3862	4550
70.1 & Up	3895	4550

* **Equipment Value Only** - Minimum Assessment for any well in production.

Formula: Amount per barrel X A.D.P. x percent % of Interest = Assessed Value

Example: \$3895 X 70.1 bbls. X .875 Interest = \$238,910 Assessed Value

\$4550 X 70.1 bbls. X .125 Interest = \$39,870 Assessed Value

The value of production equipment from bottom-of-hole to Production Sales Meter is included in the "Working Interest" Assessment.

Injection systems may be eligible for the following reductions on the working interest only.

1. Water flood - up to 25% adjustment.
2. Enhanced Recovery - up to 50% adjustment.