



STATE OF OREGON
LEGISLATIVE COUNSEL COMMITTEE

May 15, 2019

Representative Christine Drazan
900 Court Street NE H388
Salem OR 97301

Re: Cap-and-trade auction proceeds related to natural gas and Article VIII, section 2 (1)(g)

Dear Representative Drazan:

You asked the following two questions related to House Bill 2020.

First question

In an opinion addressed to you dated March 20, 2019, we concluded that a court would likely hold that proceeds the state receives pursuant to HB 2020 from the sale at auction of allowances related to motor vehicle fuel constitute "revenue from . . . [a] tax levied . . . with respect to, or measured by[,] the . . . use . . . of motor vehicle fuel" subject to Article IX, section 3a, of the Oregon Constitution. Article IX, section 3a, restricts the use of such revenue to certain specified highway-related activities.

You now ask whether it is consistent with that opinion to conclude that proceeds that the state receives pursuant to HB 2020 from the sale at auction of allowances related to natural gas constitute "proceeds from any tax or excise levied on, with respect to or measured by the extraction, production, storage, use, sale, distribution or receipt of . . . natural gas and the proceeds from any tax or excise levied on the ownership of . . . natural gas" subject to Article VIII, section 2 (1)(g), of the Oregon Constitution. Article VIII, section 2 (1)(g), dedicates such proceeds to the Common School Fund.

We believe it is consistent and that a court would likely hold that at least a portion of such auction proceeds would have to be deposited in the Common School Fund. (What portion of the proceeds would be so dedicated is addressed in the answer to your second question below.)

Voters adopted Article IX, section 3a, on May 20, 1980, on referral from the Legislative Assembly.¹ On November 4, 1980, voters adopted Ballot Measure 3, also on legislative referral, which included Article VIII, section 2 (1)(g), and Article IX, section 3b, of the Oregon

¹ Ballot Measure 1 (1980); Senate Joint Resolution 7 (1979).

Constitution.² The only appellate case interpreting Article VIII, section 2 (1)(g), or Article IX, section 3b, is *Northwest Natural Gas Co. v. Frank* from 1982.³ In that case, the Oregon Supreme Court considered whether a statutorily imposed “assessment” that was computed on the basis of energy resources sold was a “tax . . . measured by the . . . sale . . . of oil or natural gas” subject to Article VIII, section 2 (1)(g), or Article IX, section 3b.⁴

A 1971 law had authorized the State Department of Energy to impose an assessment on energy resource suppliers—electric utilities, natural gas utilities and petroleum suppliers—based on the ratio of energy resources that those suppliers sold.⁵ Shortly before voters adopted Measure 3 in 1980, the Governor asked the Attorney General whether the measure would require revenues from the energy assessment to be dedicated to the Common School Fund, and the Attorney General answered yes.⁶

Aware of this possibility, the Legislative Assembly reenacted the 1971 law in 1981, providing an alternative version of the energy resource suppliers assessment based on the ratio of the suppliers’ gross receipts. The Legislative Assembly believed the gross-receipts assessment would not be subject to Article VIII, section 2 (1)(g), or Article IX, section 3b.⁷ The 1981 law also provided for direct judicial review to the Oregon Supreme Court to determine whether revenues from the 1971 assessment based on energy resources sold were constitutionally dedicated to the Common School Fund. If the court so found, the 1971 assessment law would be repealed and the alternative version automatically adopted in lieu.⁸ On review, the court held that the energy assessment did impose a “tax” measured by the sale of oil or natural gas under Article VIII, section 2 (1)(g), and, as a consequence, that at least a portion of the proceeds were dedicated to the Common School Fund.⁹

In the 1992 case *Automobile Club of Oregon v. State*, the court relied in part on *Northwest Natural Gas* to interpret the meaning of the term “tax” for purposes of Article IX, section 3a.¹⁰ In *Automobile Club*, the court considered whether an assessment on underground storage tanks was a “tax . . . measured by the . . . receipt of motor vehicle fuel.”¹¹ Following adoption of federal environmental regulations governing underground storage tanks, Oregon’s retail gas station owners faced a “potential crisis.”¹² In response, the Legislative Assembly imposed a per-gallon assessment on the deposit of motor vehicle fuel into underground storage tanks and allocated the revenues to help retail gas stations comply with the federal regulations.¹³ The 1991 law used the word “assessment” “in an apparent effort to avoid conflict with the Oregon Constitution”¹⁴ and stated that “It is the intent of the Legislative Assembly that

² Ballot Measure 3 (1980); House Joint Resolution 6 (1979). The text of Article IX, section 3b, is substantively identical to the text of Article VIII, section 2 (1)(g), without the dedication of the proceeds to the Common School Fund.

³ *Northwest Natural Gas Co. v. Frank*, 293 Or. 374 (1982).

⁴ *Id.* at 376.

⁵ *Id.*

⁶ *Id.* at 378.

⁷ *Id.* at 379-380.

⁸ *Id.* at 380.

⁹ *Id.* at 381-382.

¹⁰ *Automobile Club of Oregon v. State*, 314 Or. 479 (1992).

¹¹ *Id.* at 488-489.

¹² *Id.* at 483.

¹³ *Id.* at 481 n.1.

¹⁴ *Id.* at 484-485.

funds assessed pursuant to section 18 of this Act are not subject to the provisions of section 2, Article VIII[,], or section 3a, Article IX[,], of the Oregon Constitution.”¹⁵

The court concluded to the contrary that revenues from the assessment were subject to the highway-related use restrictions of Article IX, section 3a.¹⁶ As the court explained, “The people of Oregon have directed that all government revenues from motor vehicle fuel taxes be expended for specified highway purposes; we must honor that direction.”¹⁷ Consequently,

We hold that the underground storage tank assessment is a “tax” under Article IX, section 3a(1)(a), and that, no matter what label the legislature may attach to a tax on motor vehicle fuel, whether it be “fee,” “excise,” “tithing,” “assessment,” or some other term, the revenues derived therefrom must be dedicated to the listed purposes.¹⁸

According to the court, *Northwest Natural Gas*, “[a] case deciding whether an assessment was a tax under a funding-dedication provision comparable to Article IX, section 3a [i.e., Article VIII, section 2 (1)(g)], supports our conclusion.”¹⁹ That is:

The “assessment” (rather than “tax”) label attached by the legislature to the charge for filling an underground storage tank, like the label attached to the [Department of Energy] assessments in *Northwest Natural Gas Co. v. Frank* . . . is important but not dispositive on the issue of whether that assessment is a tax under Article IX, section 3a. . . . This court decided in *Northwest Natural Gas Co. v. Frank* . . . that a fee imposed by government may be a “tax” in certain constitutional contexts despite the fact that the fee is called an “assessment” and that it burdens those benefited.²⁰

In sum, we believe a court would conclude that voters likely understood the term “tax” to have the same meaning in Article VIII, section 2 (1)(g), and Article IX, section 3a, which have parallel histories and effects. Both were referred by the 1979 Legislative Assembly²¹ and adopted by voters in 1980,²² and Article VIII, section 2 (1)(g), refers to Article IX, section 3a, to resolve a potential overlap in their applications.²³ In addition, the provisions are similarly restrictive in nature, constitutionally dedicating certain revenues to specified public purposes, i.e., the funding of public schools and public highways. Finally, the Oregon Supreme Court relies

¹⁵ Section 20(1), chapter 863, Oregon Laws 1991.

¹⁶ *Id.* at 487, 489.

¹⁷ *Id.* at 488 (emphasis omitted).

¹⁸ *Id.* at 487.

¹⁹ *Id.*

²⁰ *Id.* at 488, citing *Northwest Natural Gas Co. v. Frank*, 293 Or. 374.

²¹ House Joint Resolution 6 (1979) (Article VIII, section 2 (1)(g)); Senate Joint Resolution 7 (1979) (Article IX, section 3a).

²² Ballot Measure 3 (1980) (Article VIII, section 2 (1)(g)); Ballot Measure 1 (1980) (Article IX, section 3a).

²³ The third sentence of Article VIII, section 2 (1)(g), provides, “This paragraph does not include proceeds from any tax or excise as described in section 3[a], Article IX of this Constitution.” Consequently, revenue related to natural gas “used for the propulsion of motor vehicles,” within the meaning of Article IX, section 3a (1)(a), would be subject to the highway-related use restrictions of Article IX, section 3a, and would not be dedicated to the Common School Fund under Article VIII, section 2 (1)(g).

on its prior interpretations of a constitutional provision as context for that provision.²⁴ In *Automobile Club*, the court characterized Article VIII, section 2 (1)(g), as “comparable to Article IX, section 3a”²⁵ and relied in part on its earlier interpretation in *Northwest Natural Gas* of “tax” as used in Article VIII, section 2 (1)(g), to guide its interpretation in *Automobile Club* of “tax” as used in Article IX, section 3a.²⁶

For these reasons, we believe the Oregon Supreme Court would be following its reasoning in *Northwest Natural Gas* and *Automobile Club*—that the term “tax” should be interpreted consistently under the two constitutional sections—in holding that some portion of the proceeds that the state receives pursuant to HB 2020 from the sale at auction of allowances related to natural gas must be dedicated to the Common School Fund under Article VIII, section 2 (1)(g).

Second question

You further asked whether the second sentence of Article VIII, section 2 (1)(g), results in a ceiling or cap on the rate of taxes subject to Article VIII, section 2 (1)(g), of six percent of the market value of natural gas produced or salvaged from the earth or waters of this state.

Only the Attorney General has opined on this question. In 1980, his answer was that the provision was not restricted to natural gas produced or salvaged from the earth or waters *of this state*; in 1981, his answer was that it *was* so restricted. As the Attorney General amply demonstrates in these two opinions, however, the second sentence is highly ambiguous, making it extremely difficult to guess how a court would interpret it.

The first two sentences of Article VIII, section 2 (1)(g), provide:

The sources of the Common School Fund are:

...
After providing for the cost of administration and any refunds or credits authorized by law, the proceeds from any tax or excise levied on, with respect to or measured by the extraction, production, storage, use, sale, distribution or receipt of oil or natural gas and the proceeds from any tax or excise levied on the ownership of oil or natural gas. However, the rate of such taxes shall not be greater than six percent of the market value of all oil and natural gas *produced or salvaged from the earth or waters of this state as and when owned or produced.*

(Emphasis added.) *Northwest Natural Gas*, discussed in answer to your first question, is the only case we know of interpreting Article VIII, section 2 (1)(g). In that case, the court expressly declined “to suggest whether [Article VIII, section 2 (1)(g)] does apply only to taxes on oil and natural gas extracted within this state because this question is not necessary to our resolution of this case.”²⁷

²⁴ *Martin v. City of Tigard*, 335 Or. 444, 451 (2003).

²⁵ 314 Or. at 487.

²⁶ *Id.* at 487-489.

²⁷ *Northwest Natural Gas*, 293 Or. at 382.

Prior to *Northwest Natural Gas*, in anticipation of the approval of Article VIII, section 2 (1)(g), Attorney General James M. Brown issued an opinion on the subject, discussing nine possible interpretations of the phrases “of this state” and “when owned or produced.” The opinion tentatively puts forth two conclusions: that the value of the oil and natural gas for purposes of taxation is set at the time of production, except in the case of a tax on ownership, and “that the words ‘produced or salvaged from the earth or waters of this state’ should be treated as surplusage and disregarded.”²⁸ The latter conclusion was reached because the phrase “should not be deemed to alter the plain intent of [the first sentence]” and because the application of the phrase to the first sentence would violate the dormant Commerce Clause of the United States Constitution.²⁹ Other interpretations were “unreasonable, absurd, impossible to implement, or otherwise improbable.”³⁰

After the 1980 adoption of Article VIII, section 2 (1)(g), Attorney General Dave Frohnmayer issued an opinion that withdrew the conclusion of the 1980 opinion and did an about-face.³¹ “Disregarding other possible but far-fetched constructions discussed in the previous opinion,” the Attorney General discussed the history of the constitutional amendment and concluded that “produced or salvaged from the earth or waters of this state” should not be read *out* of the second sentence but rather read *into* the first.³² Thus, according to the most recent authority on the subject, only Oregon-produced oil and natural gas is subject to the dedication of proceeds to the Common School Fund and to the rate limitation under Article VIII, section 2 (1)(g).

We believe the 1981 Attorney General opinion is more persuasive than the 1980 opinion because of the more thorough discussion of the history of Article VIII, section 2 (1)(g), in the former. Under the 1981 Attorney General opinion, proceeds from a tax or excise levied with respect to or measured by the use of *Oregon-produced* natural gas must be dedicated to the Common School Fund and would be subject to the maximum rate. As a corollary, natural gas produced elsewhere is not so dedicated by Article VIII, section 2 (1)(g). By any reasoning, the plain text of the second sentence creates a maximum tax rate of six percent.

It would be difficult to overstate the uncertainty attending this conclusion. The 1981 Attorney General opinion is the only interpretation of the second sentence by either the judicial or executive branch of the Oregon state government, and, coming from the Department of Justice, it is not binding on any court. Moreover, in the 1981 opinion itself, the Attorney General stated, “It would . . . be unwise to rely on this opinion until it is confirmed by the court” and “Even if our earlier [1980] opinion is sustained, Art VIII, sec 2[(1)](g) of the Oregon Constitution, as enacted by Measure 3, is so ambiguous as to the method to be used in determining the maximum tax on Oregon-produced oil and natural gas, that it is incumbent upon the legislature to propose a clarifying constitutional amendment.”³³ Neither a judicial opinion nor a constitutional amendment has so far been delivered or adopted.

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²⁸ 41 Op. Att’y Gen. 204, 208-209 (1980).

²⁹ *Id.* at 209.

³⁰ *Id.*

³¹ 41 Op. Att’y Gen. 552, 557 (1981).

³² *Id.* at 554-557.

³³ *Id.* at 557.

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Very truly yours,

DEXTER A. JOHNSON
Legislative Counsel

A handwritten signature in cursive script that reads "Alan S Dale". The signature is written in black ink and is positioned above the typed name and title.

By
Alan S. Dale
Senior Deputy Legislative Counsel