



MEMORANDUM

Date: June, 15 2017
To: Gavin Clarkson
From: Cota Holdings, TechSource

RE: State tax burden on energy production on New Mexico Tribal lands

Gavin –

As part of our exciting conversations, I wanted to inform you as a specific Tribal instance where a Tribe that is heavily associated with the Cotton Petroleum case in the Four Corners. This particular Tribe was approached by a well-known developer with capacity, investment and production capability on a more than \$100M partnership. This particular partnership would require a Tribal "tax holiday" to assure the sustainable economics of the project. Needless to say, the Tribe was not in a position to grant a tax holiday but rather insinuated that the state should be in the position for a tax holiday nor the Tribe. This deal did not happen due to the triple tax imposed upon Indian Energy. The Cotton Petroleum case is referenced in the memo below-

The largest oil and gas producing Tribes in New Mexico are the Navajo and the Jicarilla Apache Nations with extensive landholdings in one of the oldest and richest natural gas fields in the country - the San Juan Basin. The Southern Ute and Ute Mountain Ute also have extensive oil and gas assets within the Basin, but are headquartered in Southern Colorado. The Navajo and Jicarilla Nations are largely dependent upon oil and gas revenue to finance Tribal operations and social programs. The Navajo Oil and Gas Company contributed over \$49.6 million in payments to the Navajo economy in 2013. Oil and gas revenues of the Jicarilla Apache Nation came to over \$3 million in 2014. Due to recent price declines in that sector, Jicarilla Apache Nation revenues have been reduced by over 40%. The Navajo are facing a fiscal crisis from declining oil and gas revenues in addition to reduced demand for coal and the closure or cutback of regional coal power generating stations.

The vast bulk of oil and gas production on New Mexico Reservation land comes from oil companies that lease land and invest in drilling and production. Oil and gas operators on Tribal land are triple taxed – paying federal, state and Tribal taxes – making oil and gas production on Tribal land the most expensive to operate and the first to be shut down when prices decline.

The Jicarilla Apache Nation fought for the right to charge Tribal tax on their own land, and won a landmark case before the Supreme Court in 1989 (Cotton Petroleum vs State of New Mexico), that impacted all Tribes, in which Cotton Petroleum challenged the right of Tribes to collect severance tax on production on their own land since the company was already paying State tax. The Court held in favor of the Tribe which was a boon to Tribal financial resources, but also institutionalized double taxation. In 1982 (Jicarilla Apache Tribe v. Merrion) the U.S. Supreme Court had recognized the Nation's inherent right to regulate lands and resources within the Reservation, and upheld the sovereign authority of the Tribe to impose severance tax on the production of oil and gas resources.

In New Mexico, the total state tax burden on Tribal oil and gas production is roughly 12%, which is almost as much as the royalty percentage charged by the Jicarilla Apache Nation of 16.7%. Tribal tax by contrast is roughly 10%. Combined royalty and tax payments amount to over 30% of production costs on Jicarilla Apache Tribal oil and gas production and is similar on the Navajo Reservation. This structure puts Tribes at a distinct competitive disadvantage vis-à-vis companies operating on federal or private land.

Exactly like other governments, tax revenue is essential to sustained Tribal investments in education, law enforcement, health care, and other functions. However, state governments have steadily encroached upon Tribal jurisdiction. Tribal governments lack parity with states, local governments, and the federal government in exercising taxing authority. For example, Tribes are unable to levy property taxes because of trust status of their land. Most reservations are plagued with disproportionately high levels of unemployment and poverty. As a result, Tribes are unable to establish a strong tax base structured around income taxes typically found at the local state government level, and Tribes do not impose income taxes on Tribal members. To the degree that they are able, Tribes use sales and excise taxes, but these do not generate enough revenue to support Tribal government functions, especially when there is double taxation in place.

The Navajo of the Southwest and the Mandan, Hidatsa and Arikara Nation (MHA) of South Dakota's Bakken field are actively working to end state excise tax collection on energy production on Tribal land. The Navajo Nation cites hundreds of millions of dollars in tax revenues on their energy production going to the states in which their reservation is located - with the Tribe getting few state services in return.¹ Oil drilling on the Indian Reservation of Fort Berthold (MHA Nation) accounts for about a third of North Dakota's total production.

The CEO of the Jicarilla Apache Nation Oil and gas development company (JAECO) estimates that over the next ten years there is potential for the Nation to earn between one half billion to one billion in new revenue from developing oil and gas resources on the southern half of the Reservation. The existence of state and Tribal double taxation will seriously impact the rate and amount of development that will occur.

¹ Valerie Volcovici, *Native American tribes decry state taxation of reservation energy project*; Reuters, January 27, 2017.