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MINERALS AUDIT PROGRAM
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facsimile transmittal

To: DAVE GUZY Fax No: (303) 231-3385
From: PERRY SHIRLEY Date: 5-13-98
Re: COMMENTS ON Pages: 4 + cover
CC: PROPOSED RULE

Urgent For Review Please Comment Please Reply

Notes: Originals are in the mail

PLEASE CALL (520) 871-6340 IF THERE IS A PROBLEM WITH THIS TRANSMITTAL

**THE
NAVAJO
NATION****Minerals Department
Minerals Audit Program****THOMAS E. ATCITY**
PRESIDENT**MILTON BLUEHOUSE, SR.**
VICE PRESIDENT

May 12, 1998

Attn: David S. Guzy
Minerals Management Service
Royalty Management Program
Rules and Procedures Staff
PO Box 25165, MS 3021
Denver, Colorado 80225-0165

RE: Advanced Notice of Proposed Rule
Valuation of Oil from Indian Leases
63 Federal Register 7089

Dear Mr. Guzy:

The Navajo Nation (Nation) welcomes the opportunity to submit the following comments on the Minerals Management Service's (MMS) Advanced Notice of Proposed Rulemaking (notice) on crude oil valuation for Indian leases.

We commend MMS's decision to include the Nation and other affected Indian tribes in its consultation process of developing the proposed regulations. Because the Nation was afforded the opportunity to provide input during the consultation process, the proposed regulations generally address Indian crude valuation issues and the viewpoints of the Indian tribes that provided input. Specifically, the Nation offers the following comments:

TRUST RESPONSIBILITY

The Federal Government must recognize its fiduciary trust responsibility in its consideration to amend its regulations regarding the valuation of crude oil produced from Indian leases. The Federal Government's trust responsibility to Indian Nations arises from Indian treaties, federal statutes, executive orders, legal decisions, and the historical relations between the United States and Indian Nations. In a broad sense, the trust responsibility derives from the United States' unique legal and political relationship with Indian Nations. In the narrow sense, the trust responsibility defines the precise legal obligations owed to Indian Nations, by the Federal government in managing the property and resources of Indian Nations. The trust responsibility imposes on the Federal Government the duty to remain faithful to, and advance the interest of Indian Nations.

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The Nation urges MMS to take into highest regard, its moral obligation to protect the mineral resources of Indian Nations in its promulgation of proposed regulations to eliminate any reliance on posted prices in the valuation of crude oil. When faced with two reasonable methods of calculating oil and gas royalties owed to Indian Nations, the Secretary of the Interior must choose the alternative that provides the greatest economic return to the Indian Nation. Jicarilla Apache Tribe v. Supron Energy Corp., 728 F.2d 1555, 1567 (10th Cir. 1984), dissenting opinion adopted as the majority opinion as modified, 782 F.2d 855 (10th Cir. 1986) (En Banc), cert. denied, 479 U.S. 970 (1986). The MMS is indeed faced with an alternative valuation method other than the posted price method which the oil industry has been utilizing since the mid-1980s. It must, therefore, amend its regulations to allow it to choose the method which will provide the greatest economic return for Indian resources. That alternative involves the capturing of bonuses being paid above posted prices which reflects the true market value, and in many cases, is not being treated as royalty bearing.

NYMEX AS A MARKET VALUE INDICATOR

The need for new regulations is clear. Current regulations are based upon a posted price valuation theory which has been proven to be a fictitious indicator of market value. In lawsuit after lawsuit, convincing evidence has surfaced that posted prices no longer reflect market price for crude oil in the United States. This under-valuation problem is not isolated to only non Indian country. The Nation, through performance of audits pursuant to a cooperative agreement with the MMS, has identified, on a limited basis, that bonuses above posted prices are being transferred among buyers and sellers of Navajo crude. However, the Nation's auditors are limited by the current regulations which place obstacles in our effort to collect the true market value of our production. Although it is the lessee's responsibility to substantiate its royalty payments, due to MMS' benchmark system, the burden of proof is shifted to the Nation and MMS to disprove a lessee's royalty value in order to collect underpaid royalties. Because the regulations directly reference posted prices as a factor for valuing Indian production under the MMS benchmark system, industry refuses to release pertinent information (i.e. buy/sell/exchange agreements, general ledger accounts, etc.) that is necessary to establish whether royalty payments reflect true market price. Reliance on statutory, regulatory and lease provisions in obtaining these records have been fruitless. In short, the need for NYMEX based pricing is appropriate, necessary, and long overdue.

The Nation believes the timing of the NYMEX application should remain as originally proposed, that is, the prompt month in effect on the first day of production. This results in valuing the current month's production at the nearest futures price.

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MAJOR PORTION VALUE CALCULATION

The Nation believes that the proposed regulations adequately address the major portion lease terms contained in its leases. Any deviation in the method of calculating major portion prices must maintain the underlying principles as provided in the proposed regulations.

EXCHANGE AGREEMENTS

The Nation's crude production is sweet with an average approximate gravity of 40 degrees and is sold deemed 40 degrees with no quality adjustment. Much of the crude is sold through exchange agreements. The greater Aneth area of the Navajo reservation produces a majority of the Nation's crude. The crude is refined at either of Giant Industries' refineries in Bloomfield or Jamestown, New Mexico. However, we continue to receive value based upon posted prices for the four corners area, while the crude is actually sold through exchange agreements referencing NYMEX prices either in Cushing or Midland with a minimal transportation deduction. The proposed regulations will ensure that the Nation will receive a fair and reasonable value for its mineral resources. Therefore, the only adjustment that may apply is a location differential. Again, the proposed regulations adequately address our concerns on location differentials.

COMPETITIVENESS OF INDIAN LEASES

Any notion that the proposed regulations will decrease leasing on Indian lands or otherwise affect the competitiveness of Indian leases is unfounded. The Nation has not entered into any standard leases which exclusively fall under the purview of MMS' valuation regulations since the Indian Mineral Development Act was passed in 1982. Furthermore, the Nation has an energy policy that is premised upon Navajo Nation control of its mineral resources. Therefore, we believe the proposed regulations will provide a fair and reasonable value for our leases which will be governed by the regulations, and there will be no negative consequences on future development of our mineral resources. Furthermore, the Nation, as a sovereignty, can negotiate directly with energy companies to develop its resources.

FORM MMS-4416 INDIAN CRUDE OIL VALUATION REPORT

The proposed Form MMS-4416 is not only necessary for the MMS to perform the major portion calculation that is an integral part of the proposed regulations, but it will also provide useful information for royalty accounting and audit purposes. However, the Form will only serve its purpose if it is timely and correctly submitted. The MMS should assess appropriate penalties when companies fail to submit the required Forms.

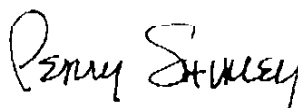
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The Nation is very dependent on the royalty revenues it receives from its non-renewable mineral resources. In fact, mineral royalty revenues account for approximately eighty percent of the Nation's annual general fund operating budget for programs which provide basic services to Navajo people. Each day that these proposed regulations are not implemented results in revenue loss which further limits the Navajo Nation Government's efforts to provide the Navajo people with basic subsistence. The Nation respectfully requests that MMS finalize and implement the amended regulations as proposed, as soon as possible.

If you have any questions, please contact me at (520) 871-6340.

Sincerely,



Perry Shirley
Assistant Director
Minerals Department

cc: Melvin Bautista, Executive Director, Division of Natural Resources, Navajo Nation
Akhtar Zaman, Director, Minerals Department, Navajo Nation