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INDIAN TAXATION OF RESERVATION MINERALS --A DOMESTIC OPEC IN THE MAKING?

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On June 25, 1876, at the Little Big Horn, Sitting Bull and Crazy Horse gave the American Indians their greatest military victory in the more than 350 years of intermittant warfare with the invading white men.[1] Just over 100 years later, on January 25, 1982, the U.S. Supreme Court gave the American Indians what promises to be their greatest legal victory, in Merrion v. Jicarilla Apache Tribe.[2] This case note analyzes Merrion, in the context of the two lines of court interpretations which it brings together.

I

In Merrion, the Court validated a tribal severance tax imposed on non-Indian lessees who were producing oil and gas on the reservation. The Jicarilla Apache reservation in northwestern New Mexico was established in 1887 by an executive order, rather than by a treaty. About 2,100 persons reside on its 742,315 acres. The Tribe is organized pursuant to the Indian Reorganization Act of 1934, and has adopted a constitution which was approved by the Secretary of the Interior in 1937. A revised constitution, which includes the power "to impose taxes and fees on non-members of the tribe doing business on the reservation"--with the approval of the Secretary, was adopted in 1968 and approved in 1969. In accordance with its revised constitution, the Tribe adopted a severance tax on oil and gas production on the reservation: $0.29 per barrel of crude oil or condensate, $0.05 per million BTU of gas. This tax was approved by the Acting Director of the Bureau of Indian Affairs, on behalf of the Secretary of the Interior, on December 23, 1976.

Two separate lawsuits were brought to enjoin the Tribe and the Secretary from enforcing the tax. The cases were consolidated, and other lessees were permitted to intervene. The U.S. District Court then permanently enjoined the

enforcement of the tax, holding that the Tribe lacked the authority to impose it; that only state and local governments had such power; and that the tax violated the Commerce Clause. Sitting en banc, the U.S. Court of Appeals reversed, with two Judges dissenting.

Merrion and the other lessee-petitioners had entered into oil and gas leases with the Tribe at various times. The 1953 lease with the Phillips Petroleum Company, for example, called for an annual rental of $1.25 per acre and a royalty of 12-1/2% of the volume or amount of all oil and gas produced on the leased land. No royalties had to be paid for oil and gas used by the lessee for development and operation of the lease. The Tribe likewise had the right to use, without charge, whatever gas it needed for schools or other tribal buildings, and to take its royalty in kind if it wished. The lease was executed for ten years, and "as much longer thereafter as oil and/or gas is produced in paying quantities from said land." Phillips is still producing under this lease.

The Phillips lease, which the Court presumed to be typical, contained no reference to the payment of taxes. The lessee does promise to comply with all existing and future regulations of the Secretary of the Interior relative to such leases: "_Provided_, That no regulation hereafter approved shall effect a change in rate or royalty or annual rental herein specified without the written consent of the parties to this lease." The lessees argue that the imposition of the severance tax adopted in 1976 would violate this clause in their leases. In dissent, Justice Stevens estimated that the tax would produce over $2,000,000 annually, on top of the $4,000,000 paid in royalties.[3]

The fundamental issue which the Court had to decide was the extent to which an Indian tribe possesses governmental sovereignty within its reservation. The majority and the dissenters proceeded from different presumptions.

The majority assumed that the tribes retain all attributes of sovereign nations except those specifically surrendered, or those inconsistent with our constitutional structure. Dissenting, Justice Stevens said that tribes had only those powers granted by treaties, or by statutes, or derived from their jurisdiction over their own members and lands. He agreed that a tribe could impose a tax as a fee or charge in return for its permission to enter onto the reservation to do business, but he said that the Jicarillas had already missed their chance to do that to these lessees. In his view, since the leases did not provide for payment of taxes to the Tribe, and since they were still binding on the Tribe, and since the Tribe had not been given the taxing power by treaty or statute, it could not now tax these non-members.[4]

Writing for the majority, Justice Marshall argued that the Tribe was sovereign within the reservation, and not only with respect to its own members. It was charged with exercising governmental functions and providing governmental services. For these purposes, the taxing power was necessary, to defray expenses. In imposing taxes, surely it could require "contributions from persons or enterprises engaged in economic activities within [its] jursidiction."[5] Here, the lessees clearly were engaging in substantial economic activities on the reservation. For Marshall, the fact that the sovereign power was also deriving revenues from these activities made no difference. "State governments commonly receive both royalty payments and severance taxes from lessees of mineral lands within their borders."[6] Marshall specifically rejected Stevens' "one-shot" theory of Indian taxation: "The fact that the Tribe chooses not to exercise its power to tax when it initially grants a non-Indian entry onto the reservation does not permanently divest the Tribe of its authority to impose such a tax."[7] Although he agrees that Indian sovereignty is "different" than that of the national, state, and local governments, he

thinks that a similar analysis is required in determining whether that different sovereign has surrendered its inherent power to tax activities within its jursidiction. For Marshall, using the leases' silence with regard to taxing power to infer a permanent waiver of the power would "turn the concept of sovereignty on its head."[8]

The majority also rejected the lessees' claim that the Jicarillas' taxing power had been divested by the legislation dealing with reservations and/or with national energy policy. The 1938 Act establishing the procedures for entering into reservation mineral leases did not do so, since it specifically preserved the tribes' power to impose regulations in accordance with their constitutions, as was done here.[9] The 1927 Act permitted state taxation of royalties from mineral production on Indian lands, but did not exclude the possibility of a concurrent tax by the tribe itself.[10] As for the claimed conflict with national energy policies, the Natural Gas Policy Act of 1978 specifically includes Indian taxes in its definition of costs which may be recovered under national pricing regulations.[11]

Finally, Marshall and the majority found that the tax here did not violate the "negative implications" of the Commerce Clause. Congress had itself recognized and provided for such Indian taxes under the statutes already discussed. Even without specific congressional authorization, the tax here meets all the requirements of the Commerce Clause. It is based on a substantial nexus, is fairly apportioned, and does not discriminate against interstate commerce. The lessees only challenged the tax under the third test, but the majority held that there was no discrimination when minerals sold on and off the reservation were treated alike. Oil and gas used by the tribe itself were exempt, but this exemption was only to avoid "administrative make-work."[12]

II

Merrion represents an important landmark in the evolution of American Indian Law. The historical record of the U.S. Government in respecting its treaties with the Indians is spotty, to say the least.[13] The unique legal status of Native Americans, and their reservations, is known by only a few specialists. Until quite recently, litigations over aspects of this special status occurred infrequently.

Court cases dealing with Indian rights increased in number and scope during the 1970's, but the results were mixed. Land claims were generally decided against the Indian claimants,[14] but financial settlements were worked out for land claims in Maine and the Black Hills.[15] Indians fared better in asserting treaty rights; tribal fishing rights were recognized in Washington and Michigan cases, for example.[16] An attempt to create a sweeping educational trust for the benefit of Indian children from the terms of the 1843 Treaty of Fort Meigs was, however, rejected by the Michigan courts.[17] Indian workers also won a significant victory when the U.S. Supreme Court upheld the constitutionality of a provision in the 1964 Civil Rights Act, Title VII, which permits preferential hiring of Indians by businesses on or near Indian reservations.[18]

The most important line of legal development came in a series of cases in which various courts recognized the special territorial status of Indian reservations. Many tribal courts have exclusive jurisdiction over areas such as family relationships, and possess limited concurrent jurisdiction with the U.S. District Courts, on other matters.[19] In a pair of very significant 1973 cases, McClanahan v. State Tax Commission of Arizona[20] and Mescalero Apache Tribe v. Jones,[21] the U.S. Supreme Court refined the constitutional limits on a state's power to tax reservation Indians.

Rosalind McClanahan, an enrolled member of the Navajo tribe, had $16.20 withheld from her paychecks for Arizona state income tax. All of her income had been earned on the reservation. After the Arizona state courts had dismissed her claim for a refund, the U.S. Supreme Court reversed. The Court said that the doctrine of Indian sovereignty no longer meant that all state actions which had any impact on the reservation or on the Indian persons residing there were automatically prohibited. The current test is whether the proposed state action substantially interferes with the tribe's status and operations as a tribe. This state income tax, if levied on resident Indians like McClanahan, would clearly do so, just as would an attempt by the state to impose its real estate taxes on reservation lands.[22]

In the other 1973 case, the taxability of a ski resort operated by the Mescalero Apache tribe was at issue. The resort was located adjacent to the reservation, on land leased from the U.S. Forest Service, by Sierra Blanca Ski Enterprises, which was chartered by the U.S. Government as an Indian corporation under the Indian Reorganization Act of 1934. New Mexico sought to collect its state sales tax ($26,086.47) on revenues generated at the resort and its state use tax ($5,887.19) on equipment which had been purchased outside the state and then installed as fixtures on the leased land. The Court held that with this combination of facts, the resort's income was subject to a state sales tax, since the revenues had been earned off the reservation and since there was no <u>specific</u> exemption for such income/sales in the 1934 Act. The policy of the 1934 Act was also to permit "Indians to enter the white world on a footing of equal competition"; it would not be equal competition to give this resort a special exemption from state sales taxes. The Court did, however, apply the specific exemption from local taxation stated in the Act for "lands"

to include an exemption from taxes for permanent fixtures installed on the land.[23]

III

Merrion also represents a reaffirmation of the U.S. Supreme Court's expanded view of the taxing power of state and local governments, which has prevailed in nearly all of the Court's tax cases since 1959. In Northwestern States Portland Cement Co. v. Minnesota,[24] despite Justice Frankfurter's fears that such taxes would truly discourage interstate business and that the courts would have difficulty in establishing logical standards for such taxation, a majority of the Supreme Court validated a state income tax imposed on a "properly apportioned" share of a corporation's interstate business income. Since Northwestern States, most constitutional challenges to state and local taxes on interstate business have been rejected.[25] Even where an apportionment formula was demonstrably irrational, a state court ruled against the plaintiff business, since the irrationality happened to work in its favor on the facts of the particular case.[26]

Several of the immediate predecessors of Merrion further extended the states' taxing powers. Especially noteworthy are two recent cases involving energy companies, Mobil Oil Corp. v. Commissioner of Taxes of Vermont[27] and Commonwealth Edison Co. v. Montana.[28]

Mobil Oil, which derived a miniscule share of its total corporate revenues from its retail sales in Vermont, sought to exclude dividends received from foreign subsidiaries from its allocable tax base for the purpose of calculating Vermont income taxes owed. Vermont, of course, maintained that all of Mobil's corporate revenues, from whatever source and in whatever form, should be included in the allocation formula. The Court approved the state's inclusion of these foreign dividends in the tax base.[29]

In 1981, the Court handed down a decision which has enormous financial implications for both energy-producing and energy-consuming states. Montana, with about one-fourth of the known U.S. coal reserves, had increased its so-called "severance tax" on coal from 34 cents per ton to a maximum rate of 30 percent of the contract sales price. Four Montana coal producers and eleven of their out-of-state utility customers challenged the validity of the new tax under the Commerce Clause and the Supremacy Clause. Specifically, the plaintiffs claimed that the tax had the effect of discriminating against interstate commerce, that it was not fairly related to the amount of state services being provided, and that it conflicted with national energy policy. The U.S. Supreme Court rejected all of these arguments. Even though some 90 percent of the coal was destined for use out of state, the Court held that there was no "discrimination" in the constitutional sense, since all coal was taxed at the same uniform rate. There was not sufficient conflict with national energy policy to invoke the Supremacy Clause, since there really was no specific national policy which was being violated and since the 1920 Mineral Lands Leasing Act specifically permitted such severance taxes. The Court made its most significant ruling in disposing of the plaintiffs' third claim. The Court declared that the amount or rate of the tax was a matter for legislative discretion, and that the legislature was not required to relate the tax rate in some way to the amount of state service which was being provided to the business activity being taxed. The tax, to be constitutionally valid, only had to be related to the extent of the taxpayers' contacts with the state. Since this tax was based on the value of the coal being extracted, it was so related, and thus valid.[30]

IV

Now in Merrion, the U.S. Supreme Court has approved the imposition of a similar severance tax by an Indian tribe for minerals taken from their reservation lands.[31] The stakes here are enormous: the 1981 World Almanac indicates "tribally-owned" land of about 40 million acres, "allotted" land of about 10 million acres, and about 3.4 million acres controlled by the Bureau of Indian Affairs.[32] Significant deposits of oil, gas, oil shale, coal, and other minerals may lie beneath some of these areas.[33] Under Merrion, the removal of any such minerals could be taxed by the appropriate Indian tribe. Under the principles developed in McClanahan and Mescalero, the states could not apply their own severance taxes (if any), nor could any Indian employees living on the reservation and working on such projects, be required to pay state income taxes.[34] Similarly, mining and drilling equipment used on such reservation projects could not be subjected to state use taxes. If any such on-reservation enterprises were operated by Indian development corporations or similar tribal entities, they could not be forced to pay state income taxes either; the Mescalero tribe had to pay such taxes because their ski resort was off the reservation.

With the current increased emphasis on development of our domestic energy resources, and with the Free World dependent on unstable sources for a number of vital strategic minerals, pressure could build rapidly for exploitation of Indian-owned mineral resources. Former Secretary of the Interior James Watt endorsed Indian economic development as one of the Department's goals: "The Indian people of America need to be given an opportunity to come full swing into America.... They need to be given an opportunity to have jobs and to develop their resources...."[35] With the Reagan Administration's

encouragement and the U.S. Supreme Court's blessing, Native Americans may at last be on the verge of the economic and spiritual renaissance so long desired.

FOOTNOTES

1. For an Indian view of the battle of the Little Big Horn, see Two Moons, "The Battle of the Little Big Horn," in Wayne Moquin and Charles Van Doren, Great Documents in American Indian History, New York: Praeger Publishers, 1973.

2. 102 S.Ct. 894 (1982).

3. Id., at 917.

4. Id., at 917-927.

5. Id., at 901.

6. Id., at 902.

7. Id., at 905.

8. Id., at 907.

9. Id., at 908.

10. Id., at 909.

11. Id., at 909.

12. Id., at 912.

13. Hoxie, Frederick E. "Red Man's Burden," 37 Antioch Rev. 326 (Summer 1979); Moquin and Doren, supra, n. 1.

14. See, e.g, "What Is a Tribe?," The Economist, (January 14, 1978), 34-35.

15. Cameron, "A Note on the Legal Status of Native Americans," Michigan Business Review, (September 1979), 27-28; Norgren and Shattuck, "Still Fighting the Indians," Juris Doctor, (October/November 1978), 30, 32, 34; Turtle Mountain Band of Chippewa Indians v. United States, 490 F.2d 935 (U.S. Ct. Claims 1974).

16. Cameron, supra, n.3; Norgren and Shattuck, supra, n.3. The first appellate court decision in the Michigan dispute was People v. LeBlanc, 223 N.W.2d 305 (Mich Apps 1974). Ten years later, the dispute is still very much alive. Opre, "Only Co-operation Can End Gillnet Mess," Detroit Free Press, (January 15, 1984), 8G. Meanwhile, the Wisconsin Chippewas did negotiate a partial settlement of their claims. "Pact with Chippewas Sets Ice Fishing Limits," Ann Arbor News, (January 29, 1984), A18.

    In Arizona, the 360 Yavapai Indians living on a small reservation refused $33 million as compensation for the flooding of 17,000 of their 25,000 acres by a proposed dam. They lobbied for relocation of the dam--and won! Wall Street Journal, (December 17, 1981), 1 and 14. See also, United States v. State of Washington, 520 F.2d 676 (U.S. Ninth Circuit 1975), cert. denied, 96 S.Ct. 877 (1976), and Nevada v. United States, 103 S.Ct. 2906 (1983).

17. *Children of the Chippewa, Ottawa and Potawatomy Tribes v. The University of Michigan*, 305 N.W.2d 5 22 (Michigan 1981). But see *United States v. Mitchell*, 103 S.Ct. 2961 (1983), holding that there is a fiduciary duty owed to the Indians by the U.S. Government.

18. *Morton v. Mancari*, 417 U.S. 535 (1974).

19. See, e.g., *Fisher v. District Court*, 424 U.S. 382 (1976); *Lohnes v. Cloud*, 254 N.W.2d 430 (N.D. 1977); *United States v. Antelope*, 97 S.Ct. 877 (1976). See also, *Oliphant v. Suquamish Indian Tribe* 435 U.S. 191 (1978); *State v. Molash*, 199 N.W.2d 591 (South Dakota 1972); *Three Affiliated Tribes v. Wold Engineering*, 321 N.W.2d 510 (N.D. 1982); *State v. Webster*, 338 N.W.2d 474 (Wisc. 1983).

20. 93 S.Ct. 1257 (1973).

21. 93 S.Ct. 1267 (1973).

22. *McClanahan v. State Tax Commission of Arizona*, *supra*, n. 20. More recently, the Supreme Court held that a state cannot enforce its fish and game laws on a reservation. *New Mexico v. Mescalero Apache Tribe*, 103 S.Ct. 2378 (1983).

23. *Mescalero Apache Tribe v. Jones*, *supra*, n. 21.

24. 358 U.S. 450 (1959).

25. The one notable exception is *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979). Even the principle of that case, that a local tax should not be permitted to interfere with a uniform foreign policy, has been undermined by the more recent decision in *Container Corp. of America v. Franchise Tax board*, 103 S.Ct. 2933 (1983).

26. *Federated Department Stores v. Gerosa*, 213 N.E.2d 677 (New York 1965).

27. 100 S.Ct. 1233 (1980).

28. *Commonwealth Edison Co. v. Montana*, 101 S.Ct. 2946 (1981).

29. *Supra*, n. 27. Cf. *Container Corp. of America*, *supra*, n. 25.

30. *Supra*, n. 28.

31. *Supra*, n. 2.

32. *The World Almanac and Book of Facts 1981*, (New York: Newspaper Enterprise Association, Inc., 1980), 461, 465.

33. "An Interview with Secretary of the Interior James Watt," *First Monday*, (January/February 1982), 27-29; Charles S. Matthews, "The Energy Countdown Book," (Shell Answer Book #27, n.d.)

34. The problem is complicated by the existence of a statute which expressly authorizes State taxation of mineral production on Indian reservations, 25 U.S.C.,S.398 c; New Mexico had been taxing the activities involved in this case under the authority granted by Congress in that 1927 Act. Merrion, at 900. Justice Marshall noted, however, that the claim of unconstitutional multiple taxation should be directed against the state tax, since the Indian tax was reaching only activities which were being conducted on the reservation, and was therefore by definition "properly apportioned." Even as to the multiple state tax, however, the case for relief is not clear, since Marshall used the phrase, "in the absence of congressional ratification" (the state tax might be invalidated under the Commerce Clause). The state tax involved here seems clearly to have been congressionally "ratified" by the 1927 Act. Merrion, at 912-913, n. 26.

35. "An Interview with Secretary of the Interior James Watt," at 29.