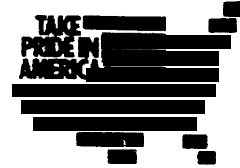




United States Department of the Interior



MINERALS MANAGEMENT SERVICE
ROYALTY MANAGEMENT PROGRAM
P.O. BOX 25165
DENVER, COLORADO 80225

IN REPLY
REFER TO:

RMP/FAD
Mail Stop 652

OCT 03 1988

Dear Payor:

The Minerals Management Service (MMS) recently reviewed tax withholdings reported nationwide for tribal and allotted Indian oil and gas leases. The tax withholdings examined are those paid to States by lessees or payors and then deducted from Indian royalty payments. This review indicates that many payors are withholding State taxes and are not using the proper tax reporting procedures for tribal and allotted Indian oil and gas leases. Based on the following analysis we believe that much of this withholding is improper.

Indian leases, with very few exceptions,^{1/} are exempt from State taxes and, consequently, no tax withholding or credits against royalties are allowed for those leases. Payors are responsible for assuring that State taxes are not assessed against exempt Indian royalties. The MMS, pursuant to the Supreme Court's Opinion in Montana v. Blackfeet Tribe, 471 U.S. 759 (1985), presumes all Indian leases to be exempt from taxes. A payor withholding taxes for Indian royalties can overcome this presumption only if it can establish that a particular Indian lease was issued under Federal statutory authority, which expressly and unambiguously subjects the Indians to State taxes for the lease revenues. Unless the lessee presents such proof, MMS will treat such withholding as deficiencies in royalty payment, and late-payment interest will be assessed as the deficient payments are collected.

Payors should review their current and past practice to determine if they have withheld taxes from royalties on tribal or allotted leases without appropriate Federal statutory authority. If taxes have been improperly withheld, then payors must submit a Report of Sales and Royalty Remittance (Form MMS-2014) correcting all such entries. If the royalties and tax credits were previously reported on Form MMS-2014 as a one-line entry net of tax, the payor must reverse the previous incorrect line and report a correcting Form MMS-2014 line for 100 percent of the royalties due. If, previously, two line entries were reported, the first as gross royalties due and the second as the tax credit, only the tax credit line must be reversed. See Chapter 4, "Adjustments, Recoupments, and Refunds," in the MMS Oil and Gas Payor Handbook for specific instructions on making correction to the Form MMS-2014. Any additional royalties due must be sent to MMS, or to the tribal lockbox established for receipt of tribal royalties, or to appropriate allottees where direct-pay provisions have been established.

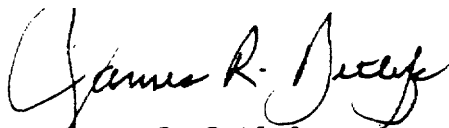
^{1/}The most notable exception is the nontax-exempt status of most Indian oil and gas leases for the five civilized tribes in Eastern Oklahoma.

You are hereby notified that MMS will be seeking the return of royalty underpayment from payors that have improperly withheld State taxes from Indian royalties. Payors withholding such taxes must be able to establish that affected lease(s) was issued under a Federal statute that expressly allows State taxation of lease royalties. If it is not clear from the statutory authority governing your lease that the Indian tax exemption has been waived, then you must presume that any withholding is improper. Those payors intending to withhold State taxes from an Indian lease, or who withheld taxes in the past and believe statutory authority justifies such withholding, may, at their option, submit their justification for withholding to MMS for review. The MMS will complete such review as expeditiously as possible, given resource constraints and the adequacy of supporting documentation provided by the payor. Payors asking for such review should be aware that any applicable interest and penalties for improperly withheld taxes will continue to run while their submission is being reviewed. Any payor requesting review should submit (a) a specific written request for a determination, (b) a complete written explanation of the basis for withholding, and (c) a copy of the lease(s). These documents should be sent to:

Mr. Vernon B. Ingraham
Chief, Office of External Affairs
Minerals Management Service
P.O. Box 25165, MS 651
Denver, Colorado 80225

Your timely adherence to instructions contained herein will minimize the need for subsequent adjustments and the payment of interest and penalties. Questions regarding Form MMS-2014 reporting issues should be addressed to your MMS Lessee Contact Branch representative at (303) 231-3288 or 1-800-525-0309.

Sincerely,



James R. Detlefs
Chief, Fiscal Accounting Division