The Federal Indian Trust Responsibility as Defined in the *U.S. v. Navajo Nation* Coal Leasing Cases

Coal Value Chain

- The coal industry is very complex. To understand the industry and the value of one's mineral interest, it is necessary to understand the coal value chain. This chain describes coal from its production to its generation of electricity or other end use and how money is made along the way by market participants. At each stage of activity – mining, processing, transporting - the product gains in value.

Peabody Energy Company

- World's largest private-sector coal company.
- In 2008, sales of 256 million tons of coal and $6.6 billion in revenues.
- Owns two mines in Arizona which are managed by Peabody Western Coal Company – the Kayenta and Black Mesa mines.

Peabody Navajo Operations

- ***Kayenta Mine***
- The Kayenta Mine is located 100 miles southwest of the Four Corners area. It sold approximately 8 million tons of coal during 2008. Kayenta Mine coal is crushed, then carried by conveyor belt to storage silos where it is loaded onto a private rail line and transported miles to the Navajo Generating Station, operated by Salt River Project near Page, Arizona.

Peabody Navajo – Hopi Operations

- ***Black Mesa Mine***
- The Black Mesa Mine, located on the Navajo and Hopi reservations in Arizona, shipped about 5 million tons of coal annually to the Mohave Generating Station near Laughlin, Nev., until the Station suspended operations in 2005 following a court settlement due to pollution violations.

Peabody Navajo - Hopi Operations

- ***Black Mesa Mine***

- Black Mesa Mine coal is crushed, mixed with water and then transported 273 miles through an underground pipeline owned by a third party. The mine and pipeline were designed to deliver coal exclusively to the Mohave Generating Station (which is operated and partially owned by Southern California Edison), which had no other source of coal.

Salt River Project

- Salt River Project ("SRP") is the nation's **third-largest public power utility**.

Southern California Edison

- Southern California Edison (SCE) is in the **top three of the United States' largest investor-owned utilities**. It is the largest electric utility in California. It is a subsidiary of Edison International.

Peabody Kayenta Coal Lease

- The coal lease between the Navajo Tribe and Sentry Royalty Company for the Kayenta Mine took effect in 1964 ("Peabody Kayenta Coal Lease"). Sentry is a wholly-owned subsidiary of Peabody. A subsidiary takes leases and then subleases them to a parent company to allow the parent company to take advantage of tax rules which lower the effective tax rate on net income for the parent company.

Bureau of Indian Affairs Lease Approval Process

- Under the Indian Mineral Leasing Act of 1938 ("IMLA"), the Bureau of Indian Affairs ("BIA") was required to approve this 1964 lease, which it did.

Indian Mineral Leasing Act of 1938

- The relevant provision of the IMLA provides as follows: "[U]nallotted lands within any Indian reservation or lands owned by any tribe . . . may, **with the approval of the Secretary of the Interior**, be leased for mining purposes, by authority of the tribal council or other authorized spokesmen for such Indians, for terms not to exceed ten years and as long thereafter as minerals are produced in paying quantities." 25 U. S. C. §396a.

DOI Coal Leasing Policy on Indian Lands Contained Fiduciary Duty

- The DOI Coal Leasing Policy, dated November 26, 1977, contained a tribal fiduciary obligation : If tribes want to pursue coal development, DOI will approve coal leasing on Indian lands where {quote}

  "(i) the tribal or individual Indian landowner desires to dispose of the coal; (ii) the terms and conditions of the lease are in the best interest of the Indian landowner; and (iii) appropriate environmental protection and reclamation safeguards are imposed on the lessee." {Close quote.}

DOI Coal Leasing Policy on Indian Lands Contained Fiduciary Duty

- {Quote} “ Such support will include detailed studies in order to prevent or minimize adverse social, cultural or other environmental impacts. It will also include technical advice and assistance to assure that such development will provide maximum long term economic benefits in terms of job opportunities and a fair monetary return reflecting the true value of their developed coal resources.” {Close quote.}

DOI Coal Leasing Policy on Indian Lands Contained Fiduciary Duty

- In using the phrase ensuring "a fair monetary return reflecting the true value of their developed coal resources" in its Policy the BIA was ahead of its time in applying a coal chain value approach. The value chain concept was popularized in 1985**. This Policy reflected the BIA's understanding that leasing does not occur in a vacuum and must consider the ultimate value of the developed coal.**

Peabody's Profit

The Peabody Kayenta Coal Lease provided for a royalty rate of 37.5 cents per ton of coal and contained a royalty adjustment clause applicable after twenty years.

Through 1983, Peabody received more than $141 million dollars from coal sales of Navajo coal production, while the Navajo Nation received less than $2.7 million in royalties for that coal.

Navajo's Request DOI to Make Royalty Rate Adjustment

In March 1984, the Navajo Nation requested that the BIA adjust the royalty rate of the Peabody Kayenta Coal Lease as negotiations regarding a royalty rate adjustment between the Navajo Nation and Peabody were not successful. The Navajo Nation did not want to miss the time requirement specified in the Kayenta Coal Lease to adjust the royalty rate.

Article VI of the Lease provides:

" [T]he royalty provisions are subject to reasonable adjustment **by the Secretary of the Interior** or his authorized representative at the end of twenty years from the effective date of this lease, and at the end of each successive ten-year period thereafter.

Navajo's Request DOI to Make Royalty Rate Adjustment

The Navajo Nation was also concerned with Peabody Kayenta Coal Lease violations regarding reclamation, rights-of-way and waste by Peabody such that lease cancellation as a warranted option was advanced by the BIA and the U.S. Geological Survey in 1979.

The 37.5 cents per ton of coal royalty under the Peabody Kayenta Coal Lease translated to a 2% royalty rate on Peabody's gross proceeds.

DOI Personnel and Agencies Responsible for Royalty Rate Adjustment

- Donald Dodge, BIA, Area Director, Navajo Area Office, Window Rock, AZ
- John N. Fritz, Acting Assistant Secretary of the Interior and Deputy Assistant Secretary – Indian Affairs (Operations), performing functions of former "Commissioner of Indian Affairs"
- Donald P. Hodel, Secretary of Interior (replaced Secretary Clark in February 1985)

DOI Personnel and Agencies Responsible for Royalty Rate Adjustment

- Frank Ryan, BIA, Director, Office of Trust Responsibility
- DOI Solicitor's Office, responsible for providing legal assistance.
- BIA Division of Energy and Mineral Resources, responsible for providing technical assistance to the BIA and tribes in leasing of energy minerals on Indian lands.
- U.S. Bureau of Mines
- U.S. Geological Survey

BIA Recommends Adjustment to 20%

- The Bureau of Mines ("BOM") performed a study of the Peabody Kayenta Coal Lease which supported a royalty rate adjustment **by the Secretary** to 20% (June 6, 1984).

- Based on this, the BIA's Area Real Property Management Officer recommended to Donald Dodge, the BIA Area Director in Window Rock, "a royalty adjustment of 20%" (June 15, 1984).

BIA Recommends Adjustment to 20%

- The BIA Division of Energy and Mineral Resources recommended 24.44%.
- The Council of Energy Resource Tribes (a non-profit in Denver, Colorado, that provides technical assistance to tribes) initially recommended a 15-20% royalty adjustment, which was later revised to 20%.

BIA Area Office Approves 20% Royalty Rate Adjustment

Donald Dodge, the Navajo Area Director, as the authorized representative of the Secretary, adjusted the royalty rate to 20%, with the concurrence of the DOI D.C. office.

Peabody Et Al Appeal

- Peabody, the Salt River Project and Southern California Edison (on behalf of themselves and the other Navajo Generating Station and Mohave Generating Station participants) then appealed the Area Director's decision to John N. Fritz, the Acting Assistant Secretary of the Interior and Deputy Assistant Secretary – Indian Affairs (Operations).

Peabody Et Al Appeal

- Peabody could have appealed through the formal appeal process through the Interior Board of Indian Appeals. It elected the informal process of appealing through the chain of command in the DOI. A decision by the Secretary or his delegated representative may be directly appealed to Federal District Court. It is thought to be quicker to appeal informally.

Peabody Et Al Appeal

- Peabody, Salt River Project and Southern California Edison collaborated on the strategy for, and handling of, the appeal.
- Their appeal challenged the timeliness of seeking the royalty rate adjustment and that the rate imposed was arbitrary, capricious and unreasonable.
- Peabody's study recommended a royalty adjustment to 5.57%-7.16% of Peabody's gross proceeds under the Peabody Kayenta Coal Lease.

DOI Acting Assistant Secretary's Review

Acting Assistant Secretary Fritz sought further technical assistance from the Bureau of Mines. He {quote} "wanted the evaluation of the economic impact to be done by somebody who had the knowledge, skills and ability to make an appropriate evaluation, and … wanted it to be as objective as possible." {Close quote.}

Royalty Rate of 20% Reasonable

- A BOM mineral economist and mining engineer collaborated on an analysis concluding that Peabody's rate of return would range from 20.1% to 32.4% if the 20% royalty rate were upheld. This compared very favorably to rates of return for other coal mining companies which ranged from 10% to 14%.
- No other study prepared by the DOI from 1984 to 1988 concluded that the 20% royalty rate was not reasonable.

Secret Peabody - DOI Secretary Negotiations

Peabody, at the direction of Southern California Edison, retained Stanley W. Hulett, a close friend and business associate of Secretary of Interior Hodel, to intercede directly with Secretary Hodel to set aside the 20% royalty adjustment and require the Navajo Nation to negotiate a deal with Peabody.

Mr. Hulett Became a Regular at DOI

- **Mr. Hulett met privately with Secretary Hodel on July 16, 1985**.

Secretarial Memo Halts Royalty Adjustment

On July 17, 1985, a Memorandum from Secretary Hodel to Acting Assistant Secretary Fritz, **as drafted by Peabody's attorneys** , directed Mr. Fritz to tell the Navajo Nation that a decision on the 20% royalty rate appeal is not imminent and for them to resolve their dispute through continued negotiation. The only change made to the Peabody draft letter was to change the word "attached" to "enclosed."

Peabody Coal Lease Amendment Negotiation Team

- Companies such as Peabody, Salt River Project and Southern California Edison each have the personnel capacity to perform such negotiations. **Here they worked together**. This capacity includes
- Executive management team
- Coal geologists and geophysicists
- Landmen
- Production engineers

Peabody Coal Lease Amendment Negotiation Team

- Hydrologists
- Procurement supply specialists
- Ph.D. Chemists specializing in the processing of production
- Transportation experts (slurry lines, railroads)
- Marketers
- Distributors (end-user)
- Safety, Health and Environmental Engineers

Peabody Coal Lease Amendment Negotiation Team

- Economists (price and cost forecasts)
- Finance and investment specialists (to advise regarding capital requirements)
- Government affairs specialists
- Public relations specialists (to deal with community problems, media, etc.)
- Human resource specialists

Peabody Coal Lease Amendment Negotiation Team

- Politically-connected lobbyists
- Specialized accountants
- Specialized in-house lawyers and outside law firms
- Tax experts
- Insurance experts
- Real property appraisers
- Right-of-way agents

Navajo Nation in 1938, 1964 and 1987 Did Not Have This Capacity

- According to the Navajo U.S. Census Statistics from 1990,
- 48.8 of the Navajo population lived below the poverty level.
- Median household income was $12,817. Per capita income was $4,788.
- 44.6% of 225,298 Navajos surveyed did not speak English well.

Navajo U.S. Census Statistics In 1990

- Not even 1% (.9) of Navajo persons surveyed aged 18-24 had a college degree.
- Only 4.5% of Navajo persons surveyed aged 24 and older had a college degree.
- Of 225,298 Navajos surveyed, 56,099 were employed. Of these only 6.2% held executive, administrative or managerial positions. 9.9% had professional specialty occupations.

DOI Knew Nation Would Get "Beat Up" by Peabody

- Acting Assistant Secretary Fritz and Director Ryan knew that the Navajo Nation could not bargain on an equal footing with Peabody. Fritz Dep. at 219-20, II App. 1127-28; Ryan Dep. at 156-61, III App. 1516-22.
- The Department also knew that the Nation would get "beat up" in negotiations with Peabody. JA 185; C.A. App. 1279-80 (Fritz), 1643-44.

Navajo Attorney General Memo of December 1985

- A Memorandum dated December 30, 1985, from the Navajo Attorney General Claudine Arthur to Tribal Chairman Peterson Zah, pointed out the many serious deficiencies in the negotiated Coal Lease Amendment.

Navajo Nation Approval Withheld Under Tribal Chairman Peterson Zah Administration

- Navajo Nation approval was withheld under Tribal Chairman Peterson Zah's administration. Tribal Chairman Zah though had campaigned in 1982 on a platform of obtaining fair coal royalties. However, he had not secured any increases as of December 1985. He lost re-election as Tribal Chairman in 1986 to Peter MacDonald.

Re-Election of Peter MacDonald Leads to Navajo Nation Approval of Coal Lease Amendment in 1987

- Re-elected Tribal Chairman MacDonald told Peabody that he wanted to wrap up negotiations on the Coal Lease Amendment. Review of the Coal Lease Amendment by BIA was requested on September 16, 1987. The BIA Assistant Area Director approved the Coal Lease Amendment on November 24, 1987.

Approval "Rubberstamping Exercise"

- No economic analysis or competent review of the Peabody Coal Lease Amendment was ever done by the DOI. This Amendment included changing not only the Peabody Kayenta Coal Lease but also the leases for the Black Mesa Mine.
- According to Frank Ryan, BIA, Director, Office of Trust Responsibility, the approval process had degenerated into a rubberstamping exercise: {quote}

  "The way this happened was, we were rubber stamping a bunch of amendments that we weren't supposed to review . . . " {Close quote.}

Approval "Rubberstamping Exercise"

- Director Ryan, in fact, refused to sign the Amendment.
- In his estimation, it would have constituted a breach of the BIA's fiduciary duty owed to the Navajo Nation.
- The DOI employee that did sign the Amendment did not know of Director Ryan's position and would not have signed it either had she known.

Peabody Submits Coal Lease Amendment to Secretary Hodel

- Peabody then submitted the Coal Lease Amendment to Secretary Hodel.

Negotiated Peabody Coal Lease Amendment Approved after Secretary Hodel-Peabody Meeting

- After meeting with Peabody executives on December 8, 1987, in a meeting arranged by the National Coal Association, Secretary Hodel formally approved the 65 page Peabody Coal Lease Amendment on December 14, 1987.
- Peabody drafted parts of the Secretarial approval document.

Breach of Fiduciary Duty Suit Filed

- The Navajo Nation filed suit in 1993 (after information regarding the “closed door” personal meetings between Peabody and Secretary Hodel surfaced bit-by-bit) seeking damages under the Indian Tucker Act (“ITA”) for an asserted breach of fiduciary duty by the Secretary in not approving a royalty rate increase to 20% and not reviewing the economic impact of the 65 page Peabody Coal Lease Amendment on the Navajo Nation.

Alleged Damages of Six Hundred Million Dollars

- The Peabody Coal Lease Amendment approved December 14, 1987, resulted in alleged damages of Six Hundred Million Dollars to the Navajo Nation.

Damages Suffered by Navajo Nation

- The amendments to the Peabody Kayenta Coal Lease and the Black Mesa leases included in the negotiation contained the following terms which were detrimental to the Navajo Nation:
- The royalty rate was set at 12.5%;
- The Area Director's decision to adjust the royalty rate to 20.0% was vacated;

Damages Suffered by Navajo Nation

- The ability to adjust the royalty rate in the future was eliminated;
- Royalty calculations were tied to then-existing rules on coal product valuation;
- The Navajo Nation was required to forego business activity and possessory interest taxes from 1978 through 1985 for Peabody and other companies;

Damages Suffered by Navajo Nation

- The Navajo Nation was required to lease an additional 90 million tons of coal to Peabody at the 12.5% royalty rate;
- The Navajo Nation was limited in its ability to impose its full possessory interest tax on 90 million tons of coal until the year 2005;

Damages Suffered by Navajo Nation

- The Navajo Nation was required to agree in the future to lease to Peabody an unidentified 2000 acres of land at an inadequate bonus of $50 per acre;
- The Navajo Nation was required to provide water at an inadequate rate of $150 per acre foot versus $600-700 received from other lessees;

Damages Suffered by Navajo Nation

- The Navajo Nation granted improvident tax waivers in a power plant lease;
- The Navajo Nation capped the total of royalties and tribal taxes at 20.5 %, including taxes on Peabody, and other entities such as Black Mesa Pipeline, Inc., or any other transporter of coal, by slurry line, railroad and related facilities;

Damages Suffered by Navajo Nation

- The Navajo Nation granted its consent to unspecified rights-of-way desired by Peabody;
- The Navajo Nation consented to assignments of the leasehold which Peabody may grant;
- The Navajo Nation diminished its own sovereignty by consenting to suits in non-Navajo courts, waiving its sovereign immunity and exhaustion of tribal remedies as a defense in such suits.

Federal Court of Claims Rules Against Navajo Nation

- The Federal Court of Claims in Washington, D.C., ruled against the Navajo Nation in its lawsuit in February 2000.
- According to the Court, the Navajo Nation failed to present statutory authority which could be fairly interpreted as mandating compensation for the government's breach of its fiduciary duties to the Navajo Nation, and therefore could not sue under the Indian Tucker Act.

Court of Appeals of Federal Circuit Rules in Navajo Nation's Favor

- The Court of Appeals of the Federal Circuit in Washington, D.C., ruled in favor of the Navajo Nation in August 2001. According to this Court, the IMLA gave the government broad control over mineral leasing on Indian lands, thus creating a fiduciary duty enforceable through suits for monetary damages.

U.S. Supreme Court Rules Against Navajo Nation in 2003

- The Supreme Court held that "the Tribe's claim for compensation . . . fails." *United States* v. *Navajo Nation*, 537 U. S. 488, 493 *("Navajo I").*
- The Court explained that to invoke the ITA and thereby bypass federal sovereign immunity, a tribe "**must identify a substantive source of law that establishes specific fiduciary or other duties**, and allege that the Government has failed faithfully to perform those duties." *Id.* at 506.

U.S. Supreme Court Rules Against Navajo Nation in 2003

- Justice Ginsburg, in her opinion stated: We construed the IMLA in light of its purpose: to "enhance tribal self-determination by giving Tribes, not the Government, the lead role in negotiating mining leases with third parties."
- The IMLA did not create, expressly or otherwise, a trust duty with respect to coal leasing and so there existed no enforceable fiduciary obligations that the tribe could sue the government for having neglected.

U.S. Supreme Court Rules Against Navajo Nation in 2003

The royalty rate adjustment clause did not require the Navajo Nation to negotiate anything.

Article VI of the Lease provides:

“ [T]he royalty provisions are subject to reasonable adjustment **by the Secretary of the Interior…**

Navajo Nation Allowed to Present Other Statutes as Mandating Compensation ("Navajo II")

- As the Court in 2003 did not analyze statutes other than the IMLA, Indian Mineral Development Act, and 25 U.S.C. §399 which also pertained to leasing, the Navajo Nation was allowed a second chance to argue any other statute that might provide a basis for damages.

NHRA and SMCRA

- The Navajo Nation argued the Navajo-Hopi Rehabilitation Act of 1950 ("NHRA") and the Surface Mining Control and Reclamation Act of 1977 ("SMCRA") created a fiduciary duty the breach of which would be compensable in money damages.

The Federal Court of Claims Again Rules Against the Navajo Nation in 2005 (Navajo II)

- The Federal Court of Claims again ruled against the Navajo Nation.

The Court of Appeals of the Federal Circuit Rules in the Navajo Nation's Favor in 2007 (Navajo II)

- This Court held that the government had violated the specific duties created by NHRA and SMCRA, as well as "common law trust duties of care, candor, and loyalty" that arise from the comprehensive control over tribal coal that is exercised by the government.

The U.S. Supreme Court Rules Against the Navajo Nation in 2009 (Navajo II)

- The U.S. Supreme Court (in a unanimous opinion) held that none of the statutes cited by the Navajo Nation provided a basis for recovery. The leases were not issued under the Navajo-Hopi Rehabilitation Act. Further, the Surface Mining Control and Reclamation Act of 1977 did not apply to the leases at hand.

U.S. Supreme Court Construed IMLA Too Narrowly

- In my opinion, the leasing and lease amendment process were wrongly construed as occurring in a vacuum and the express language requiring Secretarial approval was ignored.
- Coal management includes many processes: leasing and lease amendment processes are only a **minute, yet critical**, part of the total comprehensive control exercised by the federal government.
- This is evidenced by the government's own federal leasing process.

Federal Coal Management Program

The decades of the 1970-1980's were a prolific time period for DOI activity in federal coal management, but not Indian coal management. The Federal Coal Lease Amendments Act of 1976 was enacted. In June 1976, the Office of Minerals Policy and Research Analysis, DOI, prepared a two volume study of the Laws and Regulations Affecting Coal along with a Cost-Benefit Analysis.

Federal Coal Management Program

The Study was reviewed by the EPA, BIA, BLM, Bureau of Mines, Fish and Wildlife, U.S. Geological Survey, Mining Enforcement and Safety Administration, Office of the Solicitor and Forest Service. The intricate web of laws pertaining to the management of federal coal, including its leasing, is evidenced by the number of agencies involved in the overall process. Coal leasing does not exist in isolation.

Federal Coal Management Program

- Secretary Hodel adopted a comprehensive Federal Coal Management Program in February 1986. It addressed regional goals, leasing targets, land use planning, activity planning, pre-sale and sale procedures and NEPA compliance.

Federal Coal Management Program

- The Office of Surface Mining issued a Surface Mine Operator's Manual in 1983 with specific, detailed requirements for Mine Site Preparation, Mine Site Operation, Mine Site Reclamation, down to the posting of signs on the perimeter of the site and at accesses to the mine.

Self-Determination Favored but Not at Expense of Tribes

- While self-determination is favored by tribes it cannot come at the expense of its members who must rely on experts
  - **they may not understand or trust or**
  - **know they need or**
  - **can't afford or**
  - **are unable to understand the need for the compensation required to secure this expertise**
  - **don't know how to locate or**
  - **are not available or**
  - **do not want to represent tribes or**
  - **are a low priority to expert's business or**
  - **put their self-interest ahead of the tribe's.**

Life-of-Mine Permit Issued in December 2008 to Merge Kayenta and Black Mesa Mines, Appealed by Environmental Groups

- The Office of Surface Mining issued the subject Permit in the waning days of the Bush administration. It has been appealed.

Current Analysis Needed

- A coal value chain analysis is even more critical and urgent today as is an analysis of the life-of-mine permit to assure that the Navajo people are protected and receive appropriate compensation for their coal resources.

- **Thank you for coming.**

- **Please feel free to ask any questions.**