

MINUTES OF THE MEETING  
TAXATION COMMITTEE  
MONTANA STATE SENATE

January 13, 1987

The fourth meeting of the Senate Taxation Committee was called to order at 8:00 A.M. on January 13, 1987 by Chairman George McCallum in Room 413/415 of the Capitol Building.

ROLL CALL: All members were present with the exception of Senator Hager.

CONSIDERATION OF SB 45: Senator Williams, Senate District 15, presented this bill to the committee. He advised that this bill is an act to subject the gross proceeds of gemstone mines to taxation and setting the taxable percentage rate applicable to gemstone mines at 45 percent of gross proceeds. The Department of Revenue has reviewed this bill and they do have a few minor amendments that they will discuss with the committee. He stated he has no problem with the figures on the fiscal note. He advised the committee that yesterday afternoon he had received a call from an attorney representing the man who lives in Los Angeles that now has this mine. He requested that this gentleman be allowed to testify when the committee takes executive action on this bill. Everytime we do get to the point of obtaining some money from the sapphire company, all of a sudden the ownership changes or something to do with the company changes. Since 1899 there has been no tax on gemstones. If this tax is imposed this would mean about \$12,000 to the school systems and about \$50,000 to the counties. Not a large amount of money but something that should be going to the district for gems that are taken out of the mine and taxes are never being paid on them.

PROPONENTS: Representative Gene DeMars, House District 29, gave testimony in support of this bill. He stated the County Commissioners from Judith Basin have requested that he speak favorably on the bill. For the reasons outlined by Senator Williams he is in favor of this legislation.

Rich Marble, Department of Revenue, furnished the committee with technical comments concerning SB 45. His comments and proposed amendments are attached as Exhibit 1.

OPPONENTS: Lanny Perry, operates the only mine on the overdyke, gave testimony in opposition to this bill. He said he thinks everyone is in agreement that Montana needs to promote industry in the state. This bill would eliminate the opportunity for anybody to mine for gemstones. As it reads it is based on a carat rate per yard figure. The problem with this is that 50% of the total production is valueless. He showed the committee the results in gemstones from one yard of mined material. He is in favor of this bill but would like the tax rate to be fair. He referred to line 3, page 13, relating to mineral exemptions. He stated this bill is trying to base taxation on carat value on gemstones and basing exemptions on coal and materials in tons. He would propose that the exemption and taxation be based on acreage estimates. He would also amend the bill to allow the first 10,000 yards mined to be exempted from taxation. This would allow a large mining concern to come in and test without being concerned with taxation. As far as the tax being passed on gross proceeds, he has no problem with that.

Chairman McCallum advised the committee that he would allow the man who foreclosed on the Intergem Mine, who is located in California, to testify at the executive session on this bill.

QUESTIONS FROM THE COMMITTEE: Senator Crippen asked Mr. Marble if there could be a marketable value placed in the bill.

Rich Marble, Department of Revenue, said the Department does recognize the various values of the gems produced from the mine. That the sapphire chips have less value and the larger the stone the more value. We would be taking this into account under gross value by computing the sales value at production. If you are selling chips you have one value and stones and their size another value. He stated with regard to Mr. Perry's request for exemption based on yards removed that they do not object to that.

Senator Crippen said you say you will not do that but will you propose in writing a regulation to govern that what you say you will do.

Mr. Marble said it can be done and put in statute, but it only makes sense that if there is no value there will be no tax with regard to the chips.

Senator Hirsch asked Mr. Perry if he would want this written in tons.

Mr. Perry said he works in yards. The yardage figure is

more accurate and he would also tend to discourage very large indiscriminate removal because they would not be accurate.

Senator Lybeck said he had spoken with a local jeweler from his area that has been a jeweler for many years, maybe the last 30 years, and he told him that years ago he got quite a few stones out of the mines at Lewistown but now they must go to larger holders. The mines are still operating. He asked the Department of Revenue if some of the larger operators are high-grading some of the stones out of the country.

Mr. Marble said they are aware of the problem and are doing what they can to take care of the problem. One of the things discussed by Mr. Perry was the method of determining the value that comes out of the mine based on sampling and analyzing the yards removed from various segments of the mine, and would give us a better handle on what comes out of their total operation.

Senator Williams closed by stating the \$4.00 figure that was used per carat was put in the bill in 1980. He feels this figure is justified and gave figures from the "Annual Report Message" from Intergem to justify his comments. This report is attached as Exhibit 2.

CONSIDERATION OF SB 47: Senator Gage, Senate District 5, presented this bill to the committee. There has been a lot of input used in developing this bill. This bill deals with problems of jurisdiction - who has jurisdiction over what. The Solicitor of the United States of America said that Indian Governments have all the powers and responsibilities of any governmental entity within the borders of the United States and they have those powers in total except for those things that Congress has specifically denied them. To his knowledge and the knowledge of the Solicitor of the United States, Congress has never said to the Indian Nations you do not have the right to tax. Consequently, I am not sure about all reservations in the state completely, but to my knowledge, the Blackfeet Nation, which is a part of my Senate District, have been assessing tax on oil and gas. They are also planning to assess a tax on tobacco and alcohol. This bill is an attempt to put a mechanism in the state law whereby tribal governments and the government of the state of Montana can enter into agreement on the assessment and collection of all kinds of taxes. Whether that happens

it will be left up to the Indian Tribes and the State of Montana to determine whether they can actually enter into an agreement that they can both live with. All this bill does is to put that possibility into statute. There are some concerned that this bill, if tribes place a tax on property within the boundaries of the reservation, and Montana also taxes that property, that these people will be double taxed. That is not the purpose of this bill. As an example, the Indian Tribes are put into a less favorable economic situation with the 6.3% tax that the tribes levy against the oil companies. This tax is 6.3% more than the oil companies have to pay off the reservation and, of course, the oil companies will choose off the reservation when given an option. We think that with the provisions of this bill, they could enter into agreement whereby the tax would not be more than paid off the reservation and the state would agree to share a portion of tax with the tribes depending on what agreement can be worked out.

PROPOSERS: Dan Bucks, Department of Revenue, gave testimony in support of this bill. A copy of his testimony is attached as Exhibit 3.

Louis Clayborn, State Coordinator of Indian Affairs, gave testimony in support of this bill. A copy of his testimony is attached as Exhibit 4.

OPPOSERS: None.

QUESTIONS FROM THE COMMITTEE: Senator McCallum referred to page 4, lines 13-16 and asked Mr. Bucks if the Department of Revenue would be the public agency referred to.

Mr. Bucks said he believed they would be the public agency in most instances. Both the administration and the legal enactment must be lawful by both parties to this. If the language is too sparse we can work on that although he stated I believe Jim Lear has done a fine job in drafting this bill.

Senator McCallum said the legislature will become involved in passing statutes that authorize you to go ahead with a corporate agreement and you will have to decide whether to double tax.

Mr. Bucks said you can double tax but this bill provides an avenue for eliminating that. This allows us to provide, where the legislature has already enacted a tax and there is some conflict on some tax with the tribal government, a means to resolve this particular conflict.

Senator McCallum said he could see the point on oil, coal and gas but the people on the Flathead Reservation have a great deal of concern over the taxation problem and he certainly wouldn't want to vote for something that will harm them.

Senator Crippen said we are making the assumption that we will never get higher than 100%. There is nothing to prevent the state from entering into an agreement with the tribes that would end up providing more of a tax. He asked Mr. Bucks to comment.

Mr. Bucks said the problem now is we are above 100% and we do not have an avenue, absent lengthy court cases, to reduce it down to less than 100%. He would not foresee any circumstances where it would result in raising taxes beyond what had been enacted by the state and the tribes. The state could not tax more than the legislature provided for and the tribes couldn't enact more than they had enacted.

Senator Eck asked Mr. Bucks if this legislation would allow the adjustment of the tax rate, as well as to adjust the state requirements for providing services from that tax.

Mr. Bucks said this bill certainly authorizes the sharing of the revenue. In providing services from that tax the authority is already there. The agencies would certainly be involved in the discussion but not party to the agreement.

Senator Halligan asked how the tax is collected and distributed on the reservation now.

Mr. Bucks said in the case of cigarettes the wholesalers or distributors purchase stamps that are placed on the cigarettes. In the case of reservations the wholesalers are not required to purchase stamps and to place stamps on those cigarettes. We have no administrative mechanism for collecting that tax at the present time. Right now liquor does flow onto the reservation with the tax on it.

Senator Halligan asked how that revenue got back to the reservation.

Mr. Bucks said to his knowledge there is no mechanism for distributing the money. Right now there are programs that do receive some of the money.

Senator McCallum said there are cigarettes that come on the reservation that are not tax free.

Mr. Bucks said if they are purchased by non-Indian businesses on the reservation they have the tax on them.

Senator Gage closed by stating that the Indian people living on the reservation are in a peculiar situation whereby they are entitled to all of the programs that the state government has to offer in addition to jurisdiction programs of the tribal government. He does not see this as limited to state government but could see this encompassing city and county government.

Senator Mazurek asked Senator Gage if legislative approval would be necessary for the state/tribal agreements proposed.

Senator Gage said he did not anticipate that these would have to come to the legislature. He does not think that anything that is within the cooperative agreement would be in conflict with anything for the state of Montana. He would rather see it not come to the legislature.

Jim Lear asked Mr. Bucks if this would have to be noticed and adopted by the Department as a rule where there would be a hearing and review process at that time.

Mr. Bucks said he would like to consult with the Department's attorney on that. My opinion is that this is a cooperative agreement, a particular kind of document covered by this law. He stated we do have a very close communication relationship with the Oversight Committee and anything of importance ends up being reviewed by the Oversight Committee.

Hearing closed on SB 47.

FURTHER CONSIDERATION OF SB 1: Senator Mazurek made a motion that SB 1 DO PASS in light of the fact that North Dakota has enacted this compact.

Senator Neuman said he did not want to raise a strong objection but he feels that the Coal Board could be utilized instead of the commission spelled out in the bill.

Senator Mazurek said he is not sure entirely as to why the commission is used. It just is tradition carried forward from water compacts and the Coal Board may well be able to do this. North Dakota doesn't have a similar entity and this has been negotiated.

Senator Bishop is in agreement with Senator Neuman in using an existing agency and asked if a compact has to have a separate commission.

Jim Lear said the problem with that is North Dakota has already enacted substantially the same formulation that we have formed. He thinks we would have to negotiate with North Dakota to amend their law accordingly.

Senator Neuman requested that the bill be allowed to await action until Thursday.

Senator Mazurek withdrew his motion.

ACTION ON SB 47: Senator Eck made a MOTION to strike section 2 of SB 47. The motion carried.

Senator Mazurek has some concern with line 14 on page 4. He said in reading this it appears to say that it is lawfully imposed by the tribal government and public agencies. He wonders if it would be better to say lawfully administered by the tribal government and public agencies.

Senator McCallum said his concern is that this be done jointly.

Senator Eck would move that SB 47 DO PASS AS AMENDED.

Senator Hirsch also has a concern with line 14, page 4, as to whether public agencies does refer to local governments and if there should be some clarification put in the bill. His understanding is that Senator Gage's intent was to include local governments.

Jim Lear referred to section 18-11-102, MCA, which reads, "Public agency" means any political subdivision, including municipalities, counties, school districts, and any agency or department of the state of Montana."

Senator Eck's motion carried with Senator McCallum opposed.

ADJOURNMENT: There being no further business the meeting adjourned at 9:35 A.M.

  
SENATOR GEORGE MCCALLUM, Chairman

ROLL CALL

TAXATION

COMMITTEE

50th LEGISLATIVE SESSION -- 1987

Date 1-13-87

NAME	PRESENT	ABSENT	EXCUSED
SENATOR CRIPPEN	✓		
SENATOR NEUMAN	✓		
SENATOR SEVERSON	✓		
SENATOR LYBECK	✓		
SENATOR HAGER			✓
SENATOR MAZUREK	✓		
SENATOR ECK	✓		
SENATOR BROWN	✓		
SENATOR HIRSCH	✓		
SENATOR BISHOP	✓		
SENATOR HALLIGAN, VICE CHAIRMAN	✓		
SENATOR McCALLUM, CHAIRMAN	✓		

Each day attach to minutes.



DATE \_\_\_\_\_

# Taxation

SB 45  
SB 47

NAME \_\_\_\_\_

REPRESENTING

BILL #

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Support Oppo

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Dept of Revenue

SB 45

## Technical

And Corp.

*Sept 11*

SB47

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Port Harrison

County Treasurer

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John Gertney

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Dorson Morris

MACO.

SB 45  
" 47

Marvin Barber

Mont. assess

DBT only

## Driver Services

58 47

David Bechtel

## Driver Surveys

5B47

Dan Busch

POR.

SB47

D. L. Clayborn

## Indian Affairs

SR47

JOHN LAFAVER

DOR

THOMAS W MADDOX

MT. Tobacco & Candy Distributors

SB47

7

Richard Sangrey

Chippewa-Cree Tribe

5B47

✓

(Please leave prepared statement with Secretary)

Technical Comments

Possible Problem:

Definition of gemstone - could be interpreted too broadly as written.

Proposed Amendment:

1. Page 2, lines 21 and 22.

Following: "a"

Strike: "mineral or petrified material"

Insert: "sapphire, garnet, ruby or other precious or semiprecious stone"

Possible Problem:

Definition of "merchantable value" could include more than one type of gemstone.

Proposed Amendment:

Page 3, line 6

Following: "all"

Insert: "similar"

Possible Problem:

Definition of "merchantable value" is used in the definition of gross proceeds as per unit term but is an all inclusive term in other parts of the bill.

Proposed Amendment

Page 3, line 2

Following: "value"

Insert: "per carat or other unit of production"

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Possible Problem:

Catch phrase refers to gross proceeds which is not referred to in this section.

Proposed Amendment

Page 4, line 12.

Following "valuation"

Strike: "gross proceeds"

Insert: "merchantable value"

rr/93

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BILL NO. SB-45

# ANNUAL REPORT MESSAGE

We are pleased to report about the progress of Intergem. After major efforts and significant progress, we are now poised for volume and profitability.

In 1980 and 1981, the Company's activities consisted solely of limited sapphire mining operations. After formally organizing as a Limited Partnership in January 1982, we organized the mining activities, gem cutting, jewelry designs, jewelry manufacturing, financing, and initial marketing, as well as all of the required support systems. Our first jewelry pieces were sold on a test market basis in November, 1982.

1983 has been a year of implementation. Currently, over 450 jewelers in 45 states carry our product, including some of the most prestigious jewelers in the country such as Saks Fifth Avenue, May Company, H. Stern, and many others. Our sapphire/diamond line has expanded to 300 styles and is now available in untreated rubies, emeralds and all diamonds. We have added a new sapphire/pearl line and a diamond earring and pendant line. Over 350 news articles have been written about us, as we have become one of the country's prime sources for guaranteed natural gemstone jewelry.

We anticipate that 1984 will be a year of rapid expansion. We believe our 1983 gross revenues of \$1.6 million (\$1.38 million gross jewelry sales) are higher than the first year's revenues of practically any jewelry company ever organized, and we are confident that this level will be rapidly surpassed. We have

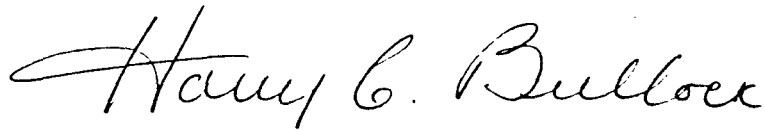
recently established gross margins of over 50 percent, so the path to profitability is sales volume. Our earnings loss of approximately \$800,000 resulted

from high initial marketing costs, investments in the future and fixed costs, which will diminish as volume increases.

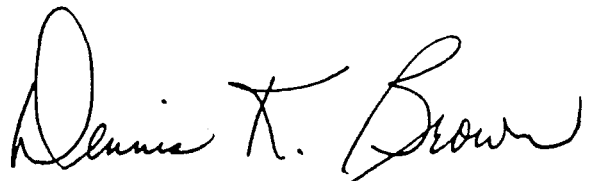
Retail jewelry chains are traditionally conservative in purchasing new concepts and pieces. They inevitably try new styles in one or two stores before expanding to 10 or 20 or to 100 or 200 over a couple of years. Approximately 50 of our current dealers are parts of very large retail chains which, when added together, consist of well over 3,000 stores. Reorders from these stores have been strong and we anticipate expansion within these chains, as well as a continued increasing number of independent jewelers and other chains.

Along with the beauty of our stones and jewelry styles, marketing program and financial terms, jewelry retailers are most interested in two issues: 1) the fact that our sapphire is American, and 2) that our stones are not treated in any way. As jewelers and consumers become more aware of the pervasive treatment of precious gems, the demand for natural, untreated stones continues to grow. This gives us a unique advantage in the marketplace.

In summary, we remain excited about Intergem, the progress which has been made, and the great opportunities ahead. The foundation has been solidly laid and the direction is clear.



Harry C. Bullock, Chairman



Dennis K. Brown, President/CEO

SENATE TAXATION

EXHIBIT NO. 2

DATE 1-13-87

BILL NO. SB45

*Full 21st*

*Can introduce up to Jan 23rd*

# THE COMPANY & COMPANY HIGHLIGHTS

Intergem, Inc., headquartered in Aurora, Colorado, is the only known fully vertically integrated precious gem and jewelry company in the world today.

The Company's integrated operations consist of sapphire mining, gemstone purchasing, faceting, jewelry designing/manufacturing and marketing the Company's Royal Gem Collection of natural sapphire, ruby, emerald and diamond jewelry.

Intergem was formed in 1980 with the purchase of the world's largest sapphire mine, known as the Yogo mine, located in central Montana. Originally organized as a limited partnership, Intergem raised over \$7.2 million from private investors and, in

March 1983, became a public company.

The blue sapphires are mined in Montana, faceted in the United States and Thailand, set in jewelry designed and manufactured in New York City, and wholesaled to retail jewelers throughout the United States.

The Company began marketing its high-quality Royal American Sapphires in fine jewelry pieces in April 1983 and, in February 1984, expanded its jewelry line to include natural, untreated emeralds, rubies and diamonds. Intergem is currently the only known jewelry company which guarantees the precious gemstones in its jewelry as completely natural and free from treatments of any kind.

Intergem owns the world's largest sapphire mine, located in Yogo Gulch, Montana, and has marketed high quality jewelry prices in its Royal American Sapphire line since April 1983.

In February 1984, Intergem introduced the Royal Gem Collection of jewelry featuring natural, untreated rubies, emeralds and diamonds in addition to its Royal American Sapphire jewelry line.

With the introduction of its Royal Gem Collection, Intergem became the largest source of guaranteed natural gemstone jewelry in the United States.

As one of the nation's only vertically integrated precious gem and jewelry companies, Intergem controls the quality of its jewelry product from the mine source through the cutting, manufacturing and wholesaling of finished jewelry pieces.

Within one year of product marketing, the number of retail jewelers carrying Intergem's jewelry line has grown to 450 retailers in 45 states and is increasing weekly.

Major jewelry retail chains and department stores which currently carry Intergem's Royal Gem Collection include:

- Saks Fifth Avenue
- The May Company
- The Denver
- Western States Jewelry
- Riddle's Jewelry
- Schwartzchild Jewelers
- H. Stern

Since Intergem became a public company in March 1983, the number of market-making firms for its common stock has quadrupled and trading volume has increased from approximately 500 to 14,000 shares per day.

Intergem is the only known jewelry company to offer a certificate of guarantee with each of its jewelry pieces. This guarantee certifies to consumers the origin and natural quality of the purchased gemstone jewelry product.

In April 1984, Intergem introduced a moderately-priced line of pearl and sapphire jewelry which is marketed directly to targeted audiences.

The majority of jewelry retail stores carrying Intergem's product line are authorized dealers, who have committed to carry a specified amount of inventory and reorder jewelry pieces sold on a monthly basis.

Intergem supplies authorized dealers with in-store display items, cooperative advertising allowances and materials and certificates of guarantee for each Royal Gem Collection piece.

Since it began marketing in April 1983, Intergem's organization and distinctive product line have been the subject of more than 350 articles, television and radio programs in national media outlets.

The international direct marketing division of Franklin Mint has scheduled a mail order promotion of a special Intergem jewelry piece for early in 1985.

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# SELECTED DATA

## SAPPHIRE INVENTORY AND RESERVES

Current inventory in-house amounts to approximately 32,000 equivalent finished carats of sapphires. An estimated additional 20,000 to 25,000 equivalent finished carats are stockpiled at the mine site for processing in 1984. A report written on March 29, 1982, by International Geoscience, a geological consulting firm, documents Intergem's probable

ore reserves as 4.2 million tons and possible ore reserves as an additional 4.5 million tons. Intergem currently recovers .5 to 1.0 finished carats per ton of ore.

During 1983, Intergem's gross sales of \$1.38 million resulted from the sale of 2,200 carats of sapphires, most of which were mounted in jewelry.

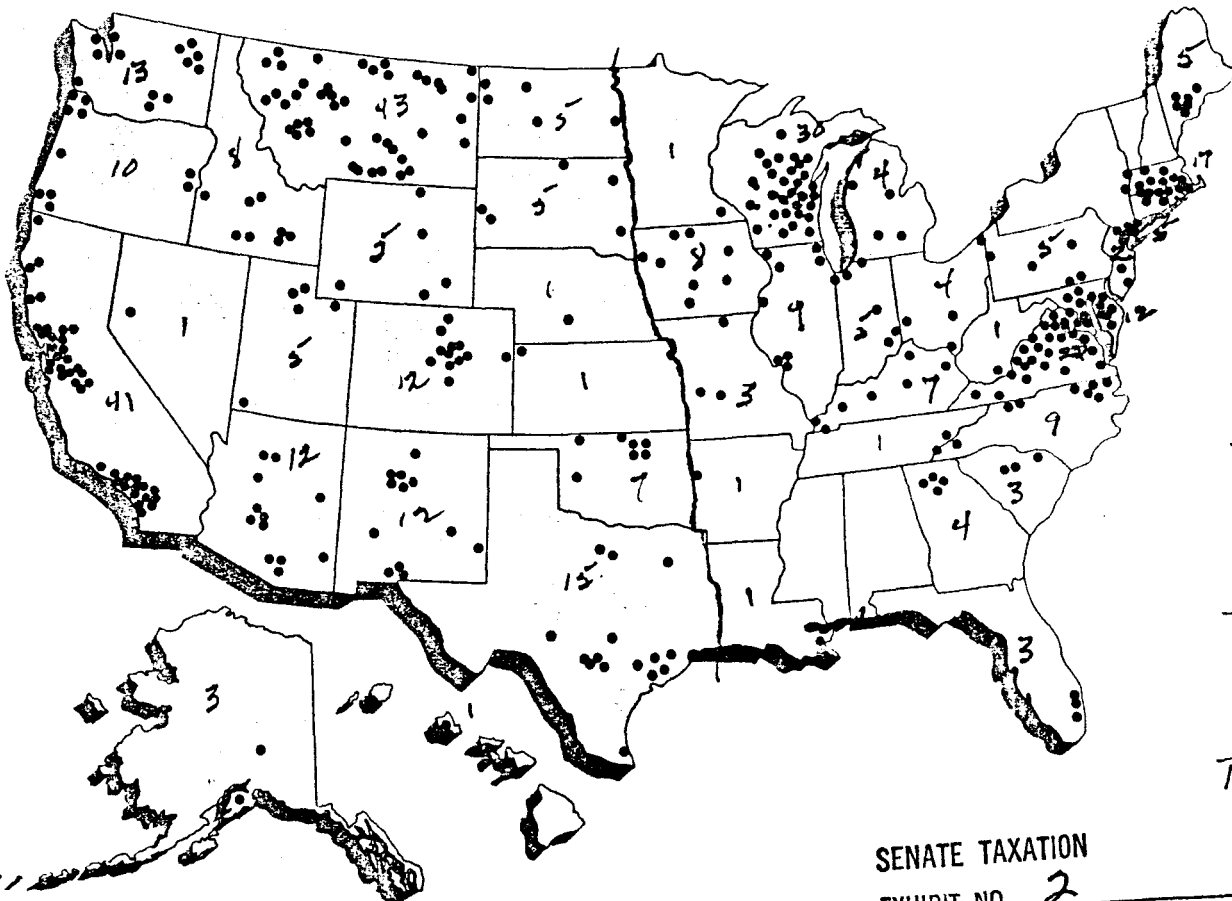
## FINANCIAL DATA

	Fiscal Year	
	1983	1982
Total Assets	\$10,401,281	\$8,898,986
Gross Revenues	1,552,553	461,103
Gross Sales	1,380,491	218,983
Net Sales or operating revenue	\$ 1,182,692	\$ 193,983
Income (loss)	\$ (818,545)	\$ (525,393).
Income (loss) per common share	\$(.05)	—
Long-term obligations	\$ 2,738,087	\$2,926,739

163  
196  
359 + 4  
Total  
363

## RETAILERS

The map below indicates the location of Intergem's current retail jeweler client base.



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# INTERGEM, INC.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### FISCAL 1982 COMPARED WITH FISCAL 1981

Since Intergem had no operating activities in 1981 and the Partnership's operating activities in 1981 were limited to mining and milling activities and no operating revenues were generated during that year, no comparative information for 1981 is provided.

### FISCAL 1983 COMPARED WITH FISCAL 1982

#### *Liquidity and Capital Resources*

Intergem's current assets consist of cash and temporary cash investments, inventory at cost, and accounts receivable.

On November 1, 1982, the Partnership obtained a \$3,000,000 line of credit, payable on demand with interest payable quarterly at a New York bank's prime rate. The line was secured with the Partnership's inventory (less consignment inventory and inventory located overseas) and current receivables. On July 1, 1983, the line was renewed at prime rate and expanded to \$5,000,000, following the completion of the annual independent appraisal of the inventory, required by the bank as part of the loan agreement. At the end of fiscal 1983, Intergem had borrowed a total of \$2,250,000 against this line, compared to \$500,000 at the end of the prior fiscal year. Most of these borrowings were used to finance additional inventory (which has grown from \$1,795,875 at the end of 1982 to \$3,122,863 at the end of 1983). The higher levels of inventory were necessary in order to provide Intergem sales representatives with a basic

display kit, and to accommodate more diverse jewelry styles and a higher level of sales. The remainder of the borrowed funds was used to finance operations.

On December 31, 1983, Intergem had \$387,476 in cash and temporary cash investments, and \$501,943 in net receivables. Most of these receivables resulted from sales made during third and fourth quarter 1983, and will be converted to cash during first and second quarter 1984.

Internal cash flow forecasts indicate that Intergem's current cash, receivables and additional borrowing capability will provide sufficient liquidity for the Company's needs during 1984 and that additional borrowings may be required, mainly to further increase inventory levels.

#### *Results of Operations*

Gross revenues from the sale of jewelry and gemstones for 1983 were \$1,380,491 compared to gross revenues of \$218,983 for 1982. The 1983 revenues were the result of approximately eight months of selling after changing manufacturing locations and most of the designs (this "retooling" effort was essentially concluded in April of 1983, when Intergem's sales representatives were issued sales kits featuring the new designs and catalogs, etc.). Sales revenues for 1982 were the result of a two month test marketing program.

The significant increase in revenues during 1983 was due mostly to the increased number of months of sales activity and the introduction of new styles, and was not a result of an increase in prices (prices were not increased during 1983).

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Most of the sales in 1983 were to retail "authorized dealer" accounts in Montana, Wisconsin, Oregon, Colorado, Virginia, Washington and the Dakotas. Intergem expects this geographical distribution to expand as new sales representatives are hired in other territories.

Sales to the retail jewelry trade are seasonal in nature, with most sales occurring during August through November. During 1983, Intergem's percentages of gross jewelry and gemstone revenues by quarter were as follows (taking into account the fact that the first quarter was atypical inasmuch as product was generally not available as a result of the retooling effort, previously discussed):

<i>Quarter Ending</i>	<i>Percent of Gross Jewelry and Gemstone Revenues</i>
March 31, 1983	8.1%
June 30, 1983	11.4%
September 30, 1983	34.2%
December 31, 1983	46.3%
	<u>100.0%</u>

Sales returns and allowances were 13 percent of Gross Jewelry and Gemstone revenues for 1983 compared to 11 percent for 1982. The 1983 percentage is higher than what Intergem expects to encounter once the Company has reached a more mature phase of market development.

General and administrative expenses were \$1,197,487 for fiscal 1983 compared to \$854,996 for fiscal 1982. The increase in general and administrative expenditures during fiscal 1983 was primarily marketing related and was necessary to introduce the product to the retail jewelry trade. Funds were used to develop product catalogs, trade advertising material and consumer oriented product information. Other significant expense areas were travel (to select a suitable U.S. manufacturing facility, to meet with large retail establishments to discuss initial promotions, and to hire and train sales representatives), salaries and sales commissions, office rent, legal and accounting services, interest expense, and depreciation, depletion and amortization.

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# INTERGEM, INC.

## BALANCE SHEETS

AS OF DECEMBER 31

ASSETS	Intergem, Inc. 1983	Intergem, Ltd. 1982
<b>CURRENT ASSETS:</b>		
Cash and temporary cash investments	\$ 387,476	\$ 1,125,140
Inventory, at cost:		
Gemstones	2,132,768	1,359,114
Jewelry	990,095	436,761
Trade accounts receivable, less allowance for sales returns and doubtful accounts of \$30,000 and \$25,000 in 1983 and 1982, respectively	501,943	125,483
	<u>4,012,282</u>	<u>3,046,498</u>
<b>PROPERTY, MINE FACILITIES AND EQUIPMENT:</b>		
Mineral rights	3,900,260	3,900,260
Deferred mine development costs	1,365,796	981,617
Mine facilities and equipment	366,260	293,142
Oil and gas properties	178,537	—
	<u>5,810,853</u>	<u>5,175,019</u>
Less—Accumulated depreciation, depletion, and amortization	<u>(150,473)</u>	<u>(59,490)</u>
	5,660,380	5,115,529
Land	544,235	545,119
	<u>6,204,615</u>	<u>5,660,648</u>
<b>OTHER ASSETS:</b>		
Design fees net of accumulated amortization of \$24,151 in 1983	96,618	120,769
Reclamation bonds and other	87,766	71,071
	<u>\$10,401,281</u>	<u>\$ 8,898,986</u>

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	Intergem, Inc. 1983	Intergem, Ltd. 1982
<b>LIABILITIES AND EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Trade accounts payable	\$ 168,037	\$ 120,640
Accrued management fee due general partner	—	63,000
Note payable to bank, including accrued interest payable of \$57,300 and \$8,715 in 1983 and 1982, respectively	2,388,714	508,715
Current portion of installment note payable, including accrued interest payable of \$98,006 and \$36,667 in 1983 and 1982, respectively	400,000	200,000
Other current liabilities	38,512	—
	<u>2,995,263</u>	<u>892,355</u>
INSTALLMENT NOTE PAYABLE, less unamortized discount of \$888,141 and \$1,143,261 in 1983 and 1982, respectively	2,676,487	2,856,739
ESTIMATED RECLAMATION LIABILITY	61,600	70,000
	<u>2,738,087</u>	<u>2,926,739</u>
<b>COMMITMENTS AND CONTINGENCIES (Note 8)</b>		
<b>EQUITY (Notes 1 and 2):</b>		
Common stock, \$.01 par value; 25,000,000 authorized; 14,940,000 issued and outstanding	149,400	—
Additional paid-in capital	6,044,206	—
Accumulated deficit, end of year	(1,525,675)	—
Total stockholders' equity	<u>4,667,931</u>	<u>—</u>
Limited partners—		
Subscribed capital	—	8,132,022
Less—Subscriptions receivable	—	(2,410,000)
	—	5,722,022
Deficit accumulated during the development stage	—	(681,670)
	—	<u>5,040,352</u>
General partner—		
Contribution	—	65,000
Deficit accumulated during the development stage	—	(25,460)
	—	39,540
Total partners' capital	<u>—</u>	<u>5,079,892</u>
	<u>\$10,401,281</u>	<u>\$ 8,898,986</u>

The accompanying notes to financial statements are an integral part of these balance sheets.

**SENATE TAXATION**

EXHIBIT NO. 2

DATE 1-13-87

SR 45

# INTERGEM, INC.

## STATEMENTS OF OPERATIONS

AS OF DECEMBER 31

	Intergem, Inc.	Intergem, Ltd.	
	1983	1982	1981
REVENUES:			
Sale of jewelry and gemstones	\$ 1,380,491	\$ 218,983	\$ —
Less—Discounts and allowances for sales returns	(197,799)	(25,000)	—
Net sales	1,182,692	193,983	—
Investment income	82,338	208,318	137,911
Oil and gas revenues, net	63,937	—	—
Gain on sale of land	18,616	16,094	—
Other	7,171	17,708	5,569
	<u>1,354,754</u>	<u>436,103</u>	<u>143,480</u>
COSTS AND EXPENSES:			
Cost of goods sold	664,465	97,196	—
General and administrative	1,197,487	854,996	205,431
Depreciation, depletion and amortization	86,254	9,304	—
Bad debt expense	43,647	—	—
Interest expense	181,446	—	—
Exploration	—	—	98,817
	<u>2,173,299</u>	<u>961,496</u>	<u>304,248</u>
NET (LOSS)	<u>\$ (818,545)</u>	<u>\$ (525,393)</u>	<u>\$ (160,768)</u>
NET (LOSS) PER SHARE (Note 3)	<u>\$(.05)</u>		
AVERAGE SHARES OUTSTANDING	<u>14,940,000</u>		

The accompanying notes to financial statements are an integral part of these statements.

SENATE TAXATION

EXHIBIT NO. 2

DATE 1-13-87

BILL NO. SB 45

# INTERGEM, INC.

## STATEMENTS OF CHANGES IN FINANCIAL POSITION

AS OF DECEMBER 31

FUNDS WERE USED FOR:	Intergem, Inc.	Intergem, Ltd.	
	1983	1982	1981
Operations—			
Net loss from operations	\$ 818,545	\$ 525,393	\$ 160,768
Less depreciation, depletion and amortization not requiring the use of funds	(86,254)	(9,304)	—
	<u>732,291</u>	<u>516,089</u>	<u>160,768</u>
Acquisition of mineral rights	—	—	3,900,260
Cost of selling limited partnership units	—	—	1,202,251
Deferred mine development costs, net of capitalized depreciation	355,299	409,190	315,298
Purchase of land, mining facilities and equipment	73,118	26,858	817,534
Reclamation bonds and other deposits	16,695	—	70,350
Acquisition of oil and gas properties	178,537	—	—
Design fees	—	120,769	—
Decrease in installment note payable	180,252	—	—
Decrease (increase) in reclamation liability	8,400	—	(70,000)
	<u>812,301</u>	<u>556,817</u>	<u>6,235,693</u>
Total funds used	<u>1,544,592</u>	<u>1,072,906</u>	<u>6,396,461</u>
FUNDS WERE PROVIDED BY:			
Acquisition of Newport, net of organization costs of merger	406,584	—	—
Cash contributions from limited partners	—	—	5,912,667
Increase in installment note payable	—	99,387	2,757,352
Other	884	27,260	4,567
	<u>407,468</u>	<u>126,647</u>	<u>8,674,586</u>
INCREASE (DECREASE) IN WORKING CAPITAL	<u>\$ (1,137,124)</u>	<u>\$ (946,259)</u>	<u>\$ 2,278,125</u>
CHANGES IN COMPONENTS OF WORKING CAPITAL:			
Increase (decrease) in current assets—			
Cash and temporary cash investments	\$ (737,664)	\$ (1,481,632)	\$ 2,127,910
Inventory	1,326,988	770,875	825,000
Mineral rights option deposit	—	—	(388,340)
Accounts receivable, net of allowances	376,460	125,483	—
	<u>965,784</u>	<u>(585,274)</u>	<u>2,564,570</u>
(Increase) decrease in current liabilities—			
Trade accounts payable	(47,397)	99,605	(165,745)
Accrued management fee due general partner	63,000	(11,875)	81,300
Current installments of note payable	(200,000)	60,000	(260,000)
Advance from general partner	—	—	58,000
Notes payable to banks	(1,879,999)	(508,715)	—
Other current liabilities	(38,512)	—	—
	<u>(2,102,908)</u>	<u>(360,985)</u>	<u>(286,445)</u>
INCREASE (DECREASE) IN WORKING CAPITAL	<u>\$ (1,137,124)</u>	<u>\$ (946,259)</u>	<u>\$ 2,278,125</u>

The accompanying notes to financial statements are an integral part of these statements.

SENATE TAXATION

EXHIBIT NO. 2

DATE 1-13-87

# INTERGEM, INC.

## STATEMENTS OF CHANGES IN EQUITY

(NOTES 1 AND 2)

	Limited Partners	General Partner
<i>INTERGEM, LTD.</i>		
BALANCE, at December 31, 1980	\$1,008,606	\$ 65,000
Original installment payments on the sale of 34.75 limited partnership units, net of related selling costs of \$1,202,251	927,749	—
Subsequent installment payments on the sale of limited partnership units	3,782,667	—
Net loss for the year ended December 31, 1981		
BALANCE, at December 31, 1981	5,719,022	65,000
Net loss for the year ended December 31, 1982		
Other	3,000	—
BALANCE, at December 31, 1982	5,722,022	65,000
<i>INTERGEM, INC.</i>		
Acquisition of Newport	—	—
Issuance of stock to partners at the time of merger	(5,722,022)	(65,000)
Organization costs of merger	—	—
Net loss for the year ended December 31, 1983		
BALANCE, at December 31, 1983	\$ —	\$ —

The accompanying notes to financial statements are an integral part of these statements.

SENATE TAXATION

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BILL NO. SB-45

Common Stock		Additional Paid-In Capital	Accumulated Deficit	Total
Shares	Amount			
—	\$ —	\$ —	\$ (20,969)	\$1,052,637
—	—	—		927,749
—	—	—		3,782,667
—	—	—	(160,768)	(160,768)
—	—	—	(181,737)	5,602,285
—	—	—	(525,393)	(525,393)
—	—	—		3,000
—	—	—	(707,130)	5,079,892
800,000	8,000	461,310		469,310
14,140,000	141,400	5,645,622		—
—	—	(62,726)		(62,726)
—	—	—	(818,545)	(818,545)
<u>14,940,000</u>	<u>\$149,400</u>	<u>\$6,044,206</u>	<u>\$(1,525,675)</u>	<u>\$4,667,931</u>

SENATE TAXATION

EXHIBIT NO. 2

DATE 1-13-87

BILL NO. SB-45

**INTERGEM,  
INCORPORATED**

**NOTES  
TO  
FINANCIAL  
STATEMENTS**

**(1) BUSINESS AND ORGANIZATION**

Intergem, Inc. (the "Company") was formed on March 25, 1983, the result of a merger between Newport Oil and Gas Incorporated ("Newport"), a Nevada corporation organized in January 1981 to engage in the oil and gas business, and Intergem, Ltd. (the "Partnership"), a Colorado limited partnership engaged in mining and marketing sapphires (Note 2). In prior years the Partnership was considered a development stage limited partnership.

The Company's principal activities now are to conduct surface and underground mining for the purpose of extracting, cutting and selling sapphires. Mining of sapphires is performed on the Company's mine property located in Judith Basin County, Montana (the "Property"). Activity through December 31, 1983, consisted of evaluation, exploration and development of underground portions of the Property, surface mining of a portion of the Property and entry into the wholesale jewelry sales market. Approximately 68,000 tons of sapphire-bearing material had been mined through December 31, 1983.

The Company markets its principal product line of jewelry called "The Royal American Sapphire," through commissioned sales representatives.

The Company is presently producing rough gemstones from surface mining techniques. However, continued operations will require, and it is the Company's plan to complete development of an underground mine. A substantial portion of the deferred development costs incurred through December 31, 1983, is applicable to the underground mine. Substantial additional funds, for which the Company has no present commitments, may be required to complete the underground mine. Recovery of these costs and the mineral rights costs is dependent upon the success of future development and underground mining of the properties.

**(2) MERGER OF NEWPORT AND THE PARTNERSHIP**

On March 25, 1983, an agreement and plan of reorganization (the "Agreement") between the Partnership and Newport was consummated. In accordance with the Agreement the Partnership transferred its business and all of its assets and existing liabilities to Newport in exchange for voting shares of Newport. Newport effected a reverse split of the then outstanding shares of Newport, reducing the outstanding shares from 8,000,000 to 800,000, and

issued 14,140,000 shares of the Company common stock to the Partnership. At that time, Newport changed its name to Intergem, Inc., the Partnership was dis-

solved and the shares distributed to its partners. The limited partners received 6,873,172 shares of Newport and the general partner and affiliates of the general partner received 7,266,828 shares. Newport shares issued to the Partnership were registered under the Securities Act of 1933 (the "Act") during 1983.

The transaction has been recorded as a reverse purchase. As a result, the Partnership's assets and liabilities as of March 25, 1983, were recorded by the Company at book value, while the assets and liabilities of Newport were adjusted to estimated fair market value at March 25, 1983.

In the course of preparing the Registration Statement for the merger, the Company's former legal counsel advised that the exemption from the registration requirements of the Act relied upon during the original sale of partnership units may not have been available. As of the date of this report the Company's current legal counsel has determined that applicable federal and state statutes of limitations would preclude any action by a vast majority of the original limited partners. The Company's management, after consultation with its legal counsel, believes the assertion of any claims that would have a material effect on the Company's financial statements is unlikely.

**(3) SUMMARY OF SIGNIFICANT ACCOUNTING  
POLICIES**

*Basis of Presentation*

The accompanying financial statements reflect the activity of Intergem, Ltd. for the years ended December 31, 1982 and 1981. The 1983 financial statements reflect the activities of the partnership through the date of merger, March 25, 1983, and the combined activities of the Company subsequent to that date.

*Exploration Costs*

Costs incurred in ascertaining the existence, location, quantity and extent of the sapphire deposits have been expensed in the period incurred. Such costs consist primarily of core drilling costs and geologists' fees.

*Deferred Mine Development Costs*

Costs incurred in preparing the Property for production have been capitalized and are shown in the accompanying financial statements as deferred

Important

mine development costs. Such costs consist primarily of engineering and geological designs and studies, environmental studies, mining studies and other carrying costs of the Property, including capitalized interest. Such costs are being amortized on a unit-of-production method as sales are made.

#### Capitalized Interest

Interest has been imputed on the noninterest bearing debt associated with the acquisition of the mineral rights. All such interest is being capitalized during the development of an underground mine on the mineral properties. As of December 31, 1983 and 1982, interest of \$691,794 and \$467,903, respectively, has been capitalized.

#### Mineral Rights

Mineral rights represent that portion of the purchase price of the Property allocated to the underlying sapphire deposits. The Company anticipates that the mineral rights will be recovered through future production and sale of gemstones. The applicable costs are being amortized on a unit-of-production method as sales are made.

#### Inventory

Gemstone inventory consists of both "rough" and "cut" sapphire gemstones, valued at cost, recovered during surface mining and during the development of the Property for future underground mining. Cost consists primarily of mining, milling and cutting costs. All general and administrative expenses are charged to operations as incurred. Inventory also includes finished jewelry, the cost of which consists primarily of gold, diamonds, the average cost of cut sapphires and manufacturing costs. Cost of sales for jewelry is determined based on the average cost per carat of sapphires and specifically identified materials and manufacturing costs. Cost of sales for cut gemstones is based on the average cost per cut carat.

The Company significantly increased inventory levels during 1983, and intends to continue to build its inventory of gemstones through its mining operations. It is not anticipated that all of the December 31, 1983, inventory will turn during 1984.

The approximate number of equivalent finished carats, based on estimated sorting and cutting yields, included in inventory at December 31, 1983, was as follows:

Rough gemstones	15,200
Cut gemstones	14,900

#### Jewelry

Total carats

2,600

32,700

#### Depreciation

Mining equipment, vehicles and facilities are depreciated on a straight-line basis over the estimated service lives of the assets ranging from three to twenty years. Depreciation costs incurred in connection with developing the Property for underground production have been capitalized as mine development costs and will be amortized on a unit-of-production method as the underlying deposits are mined and sold.

#### Net Loss Per Share

Net loss per share is computed on the basis of the weighted average number of shares of common stock outstanding since March 25, 1983. Net loss per share in 1982 and 1981 is not applicable as at that time the entity was a limited partnership. Shares obtainable through the exercise of options have not been considered as they are anti-dilutive.

#### Reclassifications

Certain reclassifications have been made to the accompanying 1982 and 1981 financial statements in order to make them comparable to the accompanying 1983 financial statements.

#### (4) NOTES PAYABLE

##### Installment Note Payable

The Property purchase contract required an initial payment in 1981 of \$1,500,000 plus accrued interest of \$112,800, with the balance of \$4,500,000 payable in semiannual installments. The amount of each installment is the greater of either \$8 per ton of sapphire-bearing ore mined and milled during the preceding six-month period, or the minimums identified on the repayment schedule below, with any unpaid balance due in May 1990.

The note payable is noninterest bearing and, accordingly, was discounted by \$1,611,164 to reflect the present value of the note based on an imputed interest rate of 10%. The related mineral rights have also been adjusted to reflect this discount.

Minimum annual installments due are as follows:

1985	\$ 500,000
1986	600,000
1987	600,000
1988	600,000

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1989	300,000
1990	964,628
Future payments due on installment note payable	3,564,628
Less—Unamortized discount at December 31, 1983	(888,141)
Long-term portion	<u>\$2,676,487</u>
Current installments due in 1984	<u>\$ 400,000</u>

After the final installment of the Property purchase contract has been paid, the Company will pay the seller of the Property a royalty for each ton of sapphire-bearing material mined and milled. The amount of the royalty will be \$4 per ton, adjusted annually for changes in the Consumer Price Index subsequent to April 1980.

#### *Line of Credit*

In July 1983, the Company renegotiated their existing line of credit and obtained a \$5,000,000 line of credit with a bank. Interest is payable monthly at Citibank's base interest rate in effect each month. The Company has the option, which it exercised in 1983, to fix the interest rate for any whole month period greater than one month, with interest paid quarterly. The fixed interest rate, adjusted quarterly, was 11% to the Company at December 31, 1983.

The Company's ability to borrow the maximum amount available under the line of credit is contingent upon its ability to furnish collateral in the form of inventories and accounts receivable at the time advances under the line of credit are requested. The Company has executed and delivered a security agreement which grants to the lender a continuing security interest in all inventory, receivables and all proceeds and products thereof.

The outstanding principal amount, payable on demand, and all accrued interest is due on May 31, 1984, when the obligation of the lender to make further advances shall expire. Management of the Company anticipates that the line of credit will be renewed during 1984. As of December 31, 1983, the Company had borrowed \$2,250,000 under this line of credit.

#### *Production Loan*

In connection with the merger (Note 2), the Company assumed a production loan payable to a bank related to oil and gas properties acquired. The outstanding principal balance and all accrued interest is due April 15, 1984. Management of the Company believes the loan will be renewed in 1984. At December

31, 1983, the principal balance was \$81,414 and was collateralized by a \$114,000 certificate of deposit.

#### (5) RELATED PARTY TRANSACTIONS

As part of the limited partnership agreement, the general partner received a management fee of \$47,500 per year for the first two years of the Partnership's activities.

A company owned by the general partner formerly supervised the mining operations, including contracting with an unrelated party for mining services, and performed milling services. The affiliated company received \$685,000 from the Partnership in 1981 and \$393,000 in 1982, including reimbursements for the third party charges. Beginning in July 1982, the Partnership began contracting mining operations with an unrelated third party.

In addition, the affiliated company charged the Partnership for general and administrative expenses, salaries and certain other direct costs incurred in connection with operating the mine and the Partnership. Such costs amounted to approximately \$215,000 in 1981 and \$296,000 in 1982. Beginning July 1982, the Partnership began paying all general and administrative expenses and salaries and such charges from the affiliated company were discontinued. General and administrative expenses of approximately \$128,000 and \$267,000 billed by the affiliated company to the Partnership in 1981 and 1982, respectively, were charged to operations in the period incurred. Direct production costs of approximately \$58,000 and \$20,000 and deferred development costs of approximately \$29,000 and \$9,000 billed by the Company in 1981 and 1982, respectively, have been capitalized.

The Partnership paid commissions of \$1,351,500 to various members of the advisory board of Intergem, Ltd., through December 31, 1981, and \$86,000 to certain limited partners for the sale of limited partnership units. These costs have been netted against limited partners' capital.

#### (6) RECLAMATION LIABILITY

The Company has an obligation to reclaim all disturbed acreage resulting from mining operations. To assure reclamation, the state of Montana requires a bond to be posted equal to its estimate of the cost of reclamation. The Company holds \$71,600 of reclamation bonds included in the accompanying balance sheets. As of December 31, 1983, management of the Company estimates the reclamation liability to be

SENATE TAXATION

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DATE 1-13-87

\$61,600, which in management's opinion, will be adequate to reclaim current disturbed acreage.

(7) COMMITMENTS AND CONTINGENCIES

As of December 31, 1983, the Company had entered into various noncancellable leases for office space and equipment. The future minimum lease payments on these leases are as follows:

<u>Year</u>	<u>Future Minimum Lease Payment</u>
1984	\$ 89,908
1985	89,908
1986	84,840
1987	54,457
1988	1,524
Total	<u>\$320,637</u>

(8) INCOME TAXES

The Company incurred an operating loss during 1983 and, accordingly, no provision for income taxes has been recorded. The estimated taxable loss of \$1,165,000 in 1983 can be carried forward to offset future taxable income. If unused, this carryforward

will expire in 1998.

The difference between the 1983 loss in the accompanying financial statements and taxable loss for 1983 is caused primarily by (a) mine development costs which are deducted currently for tax purposes and capitalized for financial statement purposes, (b) the loss attributable to the Partnership during the first quarter of 1983 and previously reported on the Partnership's final tax return, (c) mining costs which are deducted when incurred for tax purposes and included in inventory and cost of sales for financial statement purposes and (d) accelerated tax depreciation.

Certain capitalized costs in the accompanying balance sheet have a lack of tax basis resulting from the deduction of these costs on the Partnership's partners' tax returns in 1983 and earlier. These costs include mining and development costs included in deferred mine development and inventory. This lack of tax basis will result in increased provisions for income taxes for financial reporting purposes totaling approximately \$1,100,000 as inventory is sold and deferred mine development costs are amortized in future years.

SENATE TAXATION

EXHIBIT NO. 2

DATE 1-13-87

BILL NO. SB-45

REPORT  
OF  
INDEPENDENT  
PUBLIC  
ACCOUNTANTS

TO THE SHAREHOLDERS OF  
INTERGEM, INC. :

We have examined the balance sheet of INTERGEM, INC. (a Nevada corporation) as of December 31, 1983, and the related statements of operations, changes in equity and changes in financial position for the year then ended. We have also examined the balance sheet of INTERGEM, LTD. (a Colorado limited partnership in the development stage) as of December 31, 1982, and the related statements of operations, changes in equity and changes in financial position for the years ended December 31, 1982 and 1981 (see Notes 1 and 2). Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

A substantial portion of the Company's assets consists of mineral rights and deferred mine development costs, stated at cost. Recovery of the cost of these assets is dependent upon the success of future development and mining of the mineral properties.

In our auditors' report dated February 22, 1983, our opinion on the 1982 financial statements was qualified as being subject to the effect of the outcome of any unasserted claims relating to the repurchase of partnership units. As explained in Note 2, the statutes of limitations have expired on the majority of the

original partner capital contributions and management of the Company, after consultation with its legal counsel, believes the assertion of any claims that would

have a material effect on the Company's financial statements is unlikely. Accordingly, our present opinion on the 1983 financial statements, as presented herein, is no longer qualified with respect to these unasserted claims.

In our opinion, subject to the recovery of the cost of the mineral rights and deferred mine development costs as discussed previously, the financial statements referred to above present fairly, the financial position of Intergem, Inc., as of December 31, 1983, and the results of its operations and the changes in its financial position for the year then ended, and the financial position of Intergem, Ltd., as of December 31, 1982, and the results of its operations and the changes in its financial position for the years ended December 31, 1982 and 1981, in conformity with generally accepted accounting principles applied on a consistent basis.

ARTHUR ANDERSEN & CO.

Denver, Colorado,  
March 6, 1984.

SENATE TAXATION

EXHIBIT NO. 2

DATE 1-13-87

BILL NO. SB-45

TESTIMONY ON SB 47 -- STATE-TRIBAL TAX AGREEMENTS

Dan Bucks  
Department of Revenue  
January 12, 1987

*Request of Department, 12 committee*

SB 47 clarifies the State-Tribal Agreements Act by authorizing agreements for the coordination of state and tribal tax laws.

Conflicts between states and tribes over tax issues have typically been fought in the courts through lengthy and costly litigation. The cases can involve the payment of substantial funds into protest accounts instead being used for the support of services. The results of litigation are often disappointing to all the parties involved. The lengthy court battles also create uncertainties that discourage investment and economic growth.

Economic growth is also discouraged in those cases where the state and a tribe "double tax" the same activity.

In other states, cooperative agreements have proven to be an effective way of resolving state-tribal tax disputes and of preventing double taxation of citizens and businesses.

Tribal governments are turning to taxation as federal funding for tribal activities has waned. While this tribal interest in taxation creates the potential for new conflicts, it also provides an opportunity for new cooperation. The tribal need for revenue is often immediate, and as a result we do not believe that they are interested in litigation that stretches across half a decade or more. For that reason, this legislation is well-timed to prevent new conflicts and avoid new instances of double taxation.

The legislation should not, however, be oversold. Cooperative agreements provide an opportunity for resolving issues. They can work in cases where states and tribes are relatively close together in their views and there is a desire to work out differences. Where positions are far apart and strongly held, agreements are less likely to be achieved..

Examples where agreements might be used include:

- 1) the collection of taxes on reservation cigarette sales to non-Indians, and
- 2) the elimination of the double taxation of oil and gas production.

Whether agreements would ever occur in these areas depends on the willingness of the parties involved to solve these problems.

SENATE TAXATION

EXHIBIT NO. 3

DATE 1-13-87

The bill is straightforward. It directly authorizes cooperative agreements, but only in cases where the states and tribes have legally imposed taxes. The bill also provides for mechanisms for accounting for funds to be handled through cooperative agreements.

A technical amendment is needed removing Section 2 from the bill. The section refers to state suspense accounts. Because of the automation of the state accounting system, such suspense accounts are no longer used.

In summary, we believe that cooperative agreements offer an alternative to litigation as a means of resolving state-tribal tax disputes.

SENATE TAXATION

EXHIBIT NO. 3

DATE 1-13-87

BILL NO. SB-47

TESTIMONY ON SB 47  
Donald L. Clayborn, Coordinator of Indian Affairs  
January 13, 1987

Mr. Chairman, Members of the Committee:

For the record, my name is Louis Clayborn and I am the Coordinator of Indian Affairs for the state of Montana. I am here as a proponent of Senate Bill 47.

The state of Montana recognizes the inherent governmental authority of the seven (7) tribal governments that exist in Montana. As defined by the Indian Reorganization Act; i.e. the Wheeler-Howard Act of 1934; the powers of tribal government have been confirmed both in the court and by U.S. Congressional Act.

The most notable, the Indian Self-Determination Act of 1976; outlines the powers of tribal taxation that have been further defined in subsequent action by U.S. courts and interpretation of the Self-Determination Act, itself.

Tribal governments in Montana recognize their right to tax, as well as the right of the state to tax. This bill will provide for a cooperative effort; a cooperative vehicle for the sharing of revenue derived from taxation of tribal, as well as, non-tribal members within the boundaries of a reservation.

It should be noted at this point that the title of this act authorizes state and tribal cooperative agreements for assessment and collection. In no way does this act, as written, expand or diminish the revenue gathering powers of either state or tribal governments within the exterior of an Indian reservation.

Thank you for your time and if you have any further questions, please feel free to direct them to me.

SENATE TAXATION

EXHIBIT NO. 4

DATE 1-13-87

SB-47

# STANDING COMMITTEE REPORT

January 13,

19.37

MR. PRESIDENT

We, your committee on SENATE TAXATION

having had under consideration SENATE BILL

No. 47

first reading copy ( white )  
color

## STATE-TRIBAL COOPERATIVE AGREEMENTS TO ASSESS AND COLLECT TAXES

Respectfully report as follows: That SENATE BILL

No. 47

be amended as follows:

1. Title, line 11.  
Following: "15-1-501,"  
Strike: "15-1-502,"
2. Page 3, line 11 through line 3, page 4.  
Strike: Section 2 in its entirety  
Renumbe: subsequent sections
3. Page 6, line 20.  
Following: "section"  
Strike: "5"  
Insert: "4"
4. Page 6, line 22.  
Following: "section"  
Strike: "5"  
Insert: "4"

AND AS AMENDED

DO PASS

~~XXXXXXXXXX~~

SENATOR GEORGE McCALLUM,

Chairman.