



Special Report

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BRIEFLY

Under the authority of the Indian Gaming Regulatory Act, Washington tribes have opened major casinos. Recently, the profitability of these establishments has been greatly enhanced by the introduction of lottery machines. Business is booming.

Some tribes are now using casino profits to expand into other lines of business. Tribal businesses operate with regulatory and cost advantages over non-tribal businesses. Although these benefits are difficult to quantify, they provide a noticeable advantage to the tribes.

State and local governments have limited ability to collect taxes from activities on tribal lands. Money spent at non-taxed tribal businesses would, in the absence of those businesses, be spent in ways that generate state and local government revenue. The amount of foregone revenue is not trivial.

As growth management continues to restrict the availability of industrial land, urban tribes will find themselves in possession of a valuable and increasingly scarce commodity: developable property free of state and local regulations.

Untaxed and Lightly Regulated

Introduction

Indians and tribes living on recognized tribal lands occupy a very unique and complex place in the American legal landscape. The long and difficult history of relations between Indians and non-Indian settlers of North America has given rise to unpredictable, evolving and uneasy relationships between tribes and other governments.

For most of the nation's history this did not matter much. Early Supreme Court decisions mapped out a sovereign status for tribes on their lands, and the federal government protected that status. Tribes were considered exempt from nearly all state and local taxes and regulations, and while subject to federal laws, were often exempted from them too. There was little controversy over this special status because the stakes were so low. Most tribal lands had little value and few tribal enterprises made a blip on the economic screen.

In the past 30 years, this has begun to change. The rapid economic growth in the western United States has brought urban populations near to the lands of many tribes.

Tribes have begun to take advantage of their special legal status, which gives them competitive advantages in certain lines of business. The ability to avoid state tobacco taxes and fireworks regulation provided the first openings. Next tribes moved into gambling, beginning with small bingo parlors and now extending to major casinos.

For some tribes, gaming revenue has provided the capital base to expand into other lines of business. Tribes are beginning to exploit their exemptions from state taxes and regulations to compete with non-tribal businesses.

The diversion of economic activity to untaxed tribal businesses costs state and local governments revenue. Taxes on businesses account for 46 percent of state and local tax revenues in Washington state. Sales taxes collected from households by businesses are another 27 percent of state and local revenue.

In addition, non-tribal businesses that face competition from businesses on tribal lands have raised issues of fairness. How, they ask, can they compete against businesses on tribal lands when those tribes can set their own rules?

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This report provides an overview of the legal, political and economic issues surrounding tribal business enterprises, and the asymmetry between tribal lands and non-tribal lands in areas of taxes and regulation. Although many overarching issues involving the relationship between tribes and other governments have been well defined by courts, new laws and legal interpretations emerge regularly, challenging policymakers at all levels.

Tribal Sovereignty and Intergovernmental Relationships

The regulatory context within which tribal businesses operate grows out of the unique relationships that Indian tribes have with federal, state and local governments.

The regulatory context within which tribal businesses operate grows out of the unique relationships that Indian tribes have with federal, state and local governments. These relationships have been defined over the past several hundred years through the U.S. Constitution, statutes, treaties and court cases. While there is a substantial body of statutory and case law on the subject, sufficient ambiguity remains that new and important cases continue to make their way through the courts.

Indian Country

The definition of sovereignty begins with geography. The unique federal-tribal relationship is, in most respects, tied to land in what is known as “Indian Country.” (also referred to in this report as “tribal lands”). While some services may be available to individual Indians living off tribal lands, tribal sovereignty is a feature of tribal lands. Three types of land comprise Indian Country:

- ❑ *All land within the limits of any Indian reservation under the jurisdiction of the United States Government, notwithstanding the issuance of any patent, and, including rights-of-way running through the reservation.¹*

This refers to original reservation lands set aside in treaties.

- ❑ *All dependent Indian communities within the borders of the United States whether within the original or subsequently acquired territory thereof, and whether within or without the limits of a state.*

This references land occupied by a recognized tribe and land held in trust by the federal government. Although some land is taken into trust for tribes that have existing reservations, most trust land is acquired for newly-recognized tribes that have no land base.

- ❑ *All Indian allotments, the Indian titles to which have not been extinguished, including rights-of-way running through the same.*

Beginning in 1887, individual Indians could apply to be allotted or assigned parcels of reservation land by the federal government. Many of these parcels are still in the hands of Indian families and, as such, remain part of Indian Country

It is important to note the requirement that the federal government formally recognize the tribes themselves and their tribal lands. Land that is owned by a tribe or by individual Indians but does not meet one of the three definitions of Indian Country cannot be considered sovereign territory.

Evolution of tribal sovereignty

The authority of the U. S. Congress to make laws with respect to tribal members and lands is complete. The authority of state legislatures, however, is circumscribed by the concept of tribal sovereignty.

The relationship of tribes to other governments, and the primacy of the federal role, is first established in section 8 of the U.S. Constitution, as part of the commerce clause:

The Congress shall have Power To . . . regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.

And, when Washington was granted statehood, the federal government imposed a number of conditions, which are detailed in Article XXVI the state constitution, including:

That . . . unappropriated public lands . . . owned or held by any Indian or Indian tribes . . . shall remain under the absolute jurisdiction and control of the congress of the United States.

Two early court cases involving the state of Georgia and the Cherokee Tribe introduced the definition of tribes as separate sovereign governments. In *Cherokee Nation v. Georgia*, the Marshall court said that a tribe is:

a distinct political society separated from others, capable of managing its own affairs and governing itself. . . . Yet it may well be doubted whether those tribes which reside within the acknowledged boundaries of the United States can, with strict accuracy, be denominated foreign nations. They may, more correctly, perhaps, be denominated domestic dependent nations. . . . they are in a state of pupilage; their relation to the United States resembles that of a ward to his guardian.²

For over 100 years states, which had been roundly scolded in *Cherokee*, were presumed to have no autonomous power on tribal lands. More recently, however, courts have begun to recognize certain state powers. Rather than automatically referring to a general notion of sovereignty, courts now tend to look for an explicit or implicit federal preemption of state authority. Where federal law defines a federal interest or role, the matter is easy. Where there is no law, courts look for evidence of a federal interest that would preempt state jurisdiction. Courts are more likely to allow state jurisdiction in cases involving non-Indians and that do not involve internal tribal matters.

In many cases, the “preemption analysis” conducted by the courts has resulted in a bias against state authority. There are, however, a number of areas where courts have determined that state interests should override federal interests or tribal sovereignty. These include jurisdiction over crimes committed by non-Indians against other non-Indians and victimless crimes committed by non-Indians. Courts have also allowed states to regulate liquor sales on tribal lands and enforce hunting and fishing laws on tribal lands owned by non-Indians.

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Tribal sovereignty today is generally interpreted to give the presumption of authorities to tribes over their internal affairs unless specifically circumscribed by the federal government. Narrowing of sovereignty has mostly involved jurisdiction over matters somehow external to the tribe. In 1981, the Supreme Court said:

*Exercise of tribal power beyond what is necessary to protect tribal self-government or to control internal relations is inconsistent with the dependent status of the tribes, and so cannot survive without express congressional delegation.*³

In civil matters tribes retain sovereign immunity from lawsuits by state and local governments and private parties, but not from the federal government. This relationship is not reciprocal, however, as tribes cannot sue the federal government.

The Cabazon case not only defined the framework within which tribes could open high-stakes gambling operations in states that did not allow such operations, but it also established principles within which other tribal businesses operate.

The Cabazon case

The court case that has had the most far-reaching impact on Indian Country in recent years is *California v. Cabazon Band of Mission Indians*⁴. This case not only defined the framework within which tribes could open high-stakes gambling operations in states that did not allow such operations, but it also established principles within which other tribal businesses operate.

In the 1980s, the Cabazon and Morongo Bands of Mission Indians had been operating bingo parlors in Riverside County, California, which were patronized almost entirely by non-Indians (these are very small tribes). After the Cabazons began offering card games, both the state of California and Riverside County attempted to intervene and regulate both operations. The state wanted to apply its laws regulating bingo, and the county wanted to prohibit card games.

The tribes went to court, and both the Federal District Court and the Court of Appeals ruled in favor of the tribes. The case then went to the U.S. Supreme Court, which also ruled in favor of the tribes. Several key points emerged.

First and foremost, the court affirmed a previously held principle about the degree to which state laws can be enforced on tribal lands: states can enforce their criminal laws on Indian lands, but not their regulatory laws.

The central distinction in jurisdiction, then, is between a state's prohibitory/criminal laws and its regulatory/civil laws. An activity that is completely prohibited by the state is considered a criminal matter, and the state's prohibition extends to Indian Country. On the other hand, state regulation of allowed activities is a civil matter, and the state's regulations do not apply on tribal lands.

The court admitted that in California gambling fell somewhere between these two categories of law: gambling was allowed in limited circumstances, but some violations carried criminal penalties. To resolve the question of whether the tribes' activities fell under criminal/prohibitory laws or civil/regulatory laws, the court reasoned:

The shorthand test is whether the conduct at issue violates the State's public policy. . . In light of the fact that California permits a substantial amount of gambling activity, including bingo, and actually promotes gambling through its state lottery, we must conclude that

California regulates rather than prohibits gambling in general and bingo in particular.⁵

This came to be interpreted as allowing tribes to sponsor, in an unfettered way, any gambling activities that are permitted in the state under any circumstance. For example, in Washington State, tribal casinos can offer blackjack, since it is allowed at charitable “Reno night” events, but cannot have dog racing, since it is not allowed under any circumstances in the state.

Second, the court asserted a balancing of federal and state interests must be considered in determining whether state jurisdiction is preempted. Citing several federal programs that had been funding and encouraging tribal bingo operations as a useful form of economic development, the court said that:

“State jurisdiction is pre-empted . . . if it interferes or is incompatible with federal and tribal interests reflected in federal law, unless the state interests at stake are sufficient to justify the assertion of state authority.” . . . Self-determination and economic development are not within reach if the Tribes cannot raise revenues and provide employment for their members. The Tribes’ interests obviously parallel the federal interests.⁶

Third, the court drew a distinction between gambling and activities like selling tobacco and liquor. The state of California had argued that the only reason people went to tribal gaming facilities was to escape state regulations, just as they might go to a reservation to escape tobacco or liquor taxes; since the court had previously allowed states to require tribal businesses to collect state tobacco taxes from non-tribal customers, states should be able to pursue other regulation-evading actions by non-tribal members. The court rejected this reasoning, saying that:

The Tribes are not merely importing a product onto the reservations for immediate resale to non-Indians. They have built modern facilities which provide recreational opportunities and ancillary services to their patrons, who do not simply drive onto the reservations, make purchases and depart, but spend extended periods of time there enjoying the services the Tribes provide.⁷

The court had previously determined that states could tax non-value-added activities such as tobacco sales, but now explicitly asserted that states could not interfere with value-added activities. The balance of interests favors the state when tribal enterprises were simply retailing goods manufactured off of the reservation, but when goods or services are produced on the reservation, the balance favors the federal and Indian interests. This logic extends to restaurants, hotels and other facilities operated by tribes in conjunction with casinos.

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Taxes and Regulations in Indian Country

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their competitors on non-tribal lands. Questions of jurisdiction continue to be ironed out by courts as tribal, federal and state governments press their cases for authority. The current practice of seeking evidence of federal interests in order to assert federal preemption of state law applies heavily to tax and regulatory questions.

State taxation in Indian Country

As a general rule, tribal sovereignty precludes states from taxing Indian tribes and Indians themselves for property owned in and activities conducted in Indian Country. This applies to sales tax on purchases by Indians on tribal lands, motor vehicle and gas taxes, property taxes or state income taxes.

Unless otherwise preempted by federal law, however, states can tax some non-Indian activities on tribal lands, and also tax Indians living, working, owning property, or operating businesses off tribal lands. Courts have also ruled that individual Indians are only exempt from taxation for activities on lands belonging to their own tribe. Since each tribe is considered an individual sovereign nation, the privileges of sovereignty only accrue to its own members.

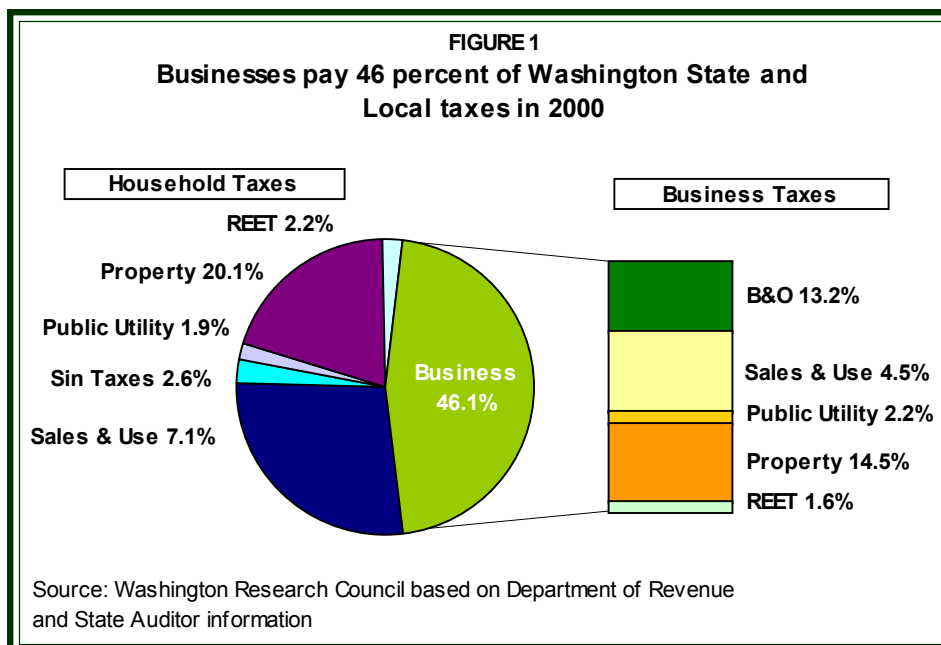
The most complex and potentially troublesome issues concern the taxation of on-reservation transactions between Indians and non-Indians.

The most complex and potentially troublesome issues concern the taxation of on-reservation transactions between Indians and non-Indians. The analysis of such transactions begins with the question: Who does the law make legally responsible for paying the tax? If the legal incidence of the tax is on the Indian, the transaction is exempt. For example, the legal incidence of Washington's retail sales tax is on buyer. The seller is acting as the agent of the state when collecting and remitting the tax. Tribal members are exempt from paying sales taxes on purchases from non-Indian retail business operating on tribal land.

If the legal incidence of the tax is on the non-Indian, the next question is whether Congress has explicitly exempted the transaction from state taxation. For example, in the case of gambling, states are explicitly prohibited from taxing non-Indian businesses that contract with tribal casinos. Finally, if not explicitly exempted, the taxability of the transaction turns on a balancing of competing federal/Indian and state interests. Consider the retail

sale of products to non-Indians by an Indian-owned retail business located on tribal land. If the products were made outside of Indian country, the state's interest in raising revenue to fund government services predominates. On the other hand, if products or services contain considerable value added on tribal lands, the federal interest in promoting tribal economic development predominates and the sales are exempt from the state's retail sales tax, as affirmed in *Cabazon*.

There is one final wrinkle: In cases where non-Indian customers are obliged to pay sales taxes, the state may have difficulty compel-



ling Indian retailers to collect and remit the tax to the state. This has frequently been the case with tobacco taxes.

Washington's state and local governments get 46 percent of their tax revenues from taxes levied on businesses. (See Figure 1.) In addition, businesses serve as governments' agents in collecting the retail sales tax, which accounts for 27 percent of state and local revenue, as well as selective sales taxes on items such as cigarettes and gasoline. Taxes collected on and through businesses do not simply fund the government services that the businesses consume: these taxes float the whole government enterprise.

Tribal businesses operate largely outside of this tax system. The expansion of tribal businesses therefore reduces the ability state and local governments to fund services.

Land use and environmental regulation

Throughout the country land use regulation remains primarily a prerogative of state and local governments, and these regulations almost never apply to developments on tribal lands. A prominent example is the "billboard alley" along I-5 through the Puyallup reservation north of Tacoma, which exists solely because state laws regulating billboards do not apply to tribal lands.⁸

The extensive and unsuccessful litigation over the White River Amphitheater near Auburn further illustrates just how little local governments can impose their will on tribal projects. Claims that the amphitheater would overload local transportation systems did not result in any mitigation requirements (the tribe has taken some voluntary measures to ease traffic congestion).

Tribal governments engage in their own land use planning (not subject to the state's Growth Management Act) and environmental review processes (not subject to the State Environmental Policy Act). They issue building permits, adopt building and development codes and perform inspections. About the only leverage state and local governments have over tribal development comes when tribes need to connect to publicly owned sewer, water or electric utilities. Governments can deny or condition such service.

Exemption from state and local land use regulation can result in significant cost savings for tribal businesses. For example,

- ❑ SEPA review and appeals on a major development on non-tribal land can cost upward of \$1 million just in consulting and legal fees, and stretch out for months or years.
- ❑ With no SEPA review, there will be no mitigation requirements, and tribes can choose whether and how to address impacts of their development.
- ❑ If they choose, tribal developments can cut costs on discretionary development standards like parking ratios, street widths, landscape requirements, design standards, etc.
- ❑ Tribal developments will pay no impact fees for local infrastructure, whether authorized through SEPA or the Growth Management Act.

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So while tribal developers often choose to engage in careful planning and review and adopt high development standards, they have the ability to adjust all those requirements to suit the economics of the project in ways that non-tribal developers cannot.

Employment Law

Employment law is a tangle of state and federal programs and regulations. In many cases states adopt programs that go beyond federal requirements and that are more expensive for businesses to comply with. While tribal businesses are subject to many, but not all, of the federal rules, they are generally exempt from state employment laws.

Unemployment insurance

In 2000 Congress passed legislation requiring employees of tribal businesses to be covered by state unemployment insurance.⁹ The Washington State Legislature implemented this requirement in 2001.¹⁰ The new law allows tribal businesses to reimburse the state system for benefits paid to former employees, instead of paying the standard payroll tax into the unemployment insurance trust fund. This option, which is not available to private businesses, can result in significant cost savings.

Tribal businesses do not have to comply with most state employment law, including workers compensation.

Workers compensation

Tribal businesses do not have to comply with most state employment law, including workers compensation. Since tribes are generally immune from lawsuits by private parties, they have had little incentive to carry the kind of industrial insurance that non-tribal businesses need to in order to insulate themselves from lawsuits.

As part of federal contracts or state gaming compacts, tribes can be required to carry industrial insurance. Many tribal businesses carry industrial insurance voluntarily, especially since the Federal Tort Claims Act can allow action for negligence by tribal employers. Tribal businesses have the option of entering into the state system through the Department of Labor and Industries. They can, however, purchase industrial insurance from private insurance providers, which is often less expensive than the state program. Non-tribal businesses in Washington do not have the option of purchasing private insurance, and only the largest employers have the option of self-insurance.

Employment discrimination

The Civil Rights Act of 1964, which prohibits employment discrimination, does not apply to tribal businesses that choose to offer employment preferences to Indians. Tribal businesses are specifically exempted from the provisions in the Americans with Disabilities Act that prohibit employment discrimination based on disabilities.

Other employment law

The extent to which tribal businesses are subject to other federal employment law – The Occupational Safety and Health Act, The Age Discrimination in Employment Act, National Labor Relations Act etc. – is not always clear. Federal courts have ruled in opposite ways. In a landmark case, *Federal Power Commission v. Tuscarora Indian Nation*¹¹ the Supreme Court stated:

It is now well settled by many decisions of this court that a general statute in terms applying to all persons includes Indians and their property interests. . . . Whenever they and their interests have been the subject affected by legislation they have been named and their interests specifically dealt with.

This logic was further refined in another widely cited case in the Ninth Circuit (which includes Washington State), *Donovan v. Coeur d'Alene Tribal Farm*.¹² In this case the court reaffirmed federal authority over tribes in general statutes, but added a three-part test of whether a tribe should be exempt from a law. A tribe would be exempt if:

- (a) The law touches exclusive rights of self-governance in purely intramural matters;
- (b) Application of the law would run contrary to treaty rights; or
- (c) Legislative history shows that Congress meant to exempt tribes.

Other courts, notably the Tenth and Eighth Circuit courts, have leaned toward tribal sovereignty and looked for clear legislative intent as to the applicability of regulations to tribes. In contrast, the Seventh and Second Circuits have adopted the *Coeur d'Alene* logic.

But even if tribal businesses are subject to federal regulations, they will not have to comply with the often more stringent and costly Washington state versions. As an example, the ergonomic rules considered by OSHA would have applied to tribal businesses, but they will not be bound the more costly rules promulgated by Washington State's Department of Labor and Industries.

So, while tribal businesses will generally comply with basic employment regulations, they enjoy more options than non-tribal businesses in the state to keep their employment costs down.

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Tribal Enterprises

Tobacco sales

As tribes moved away from resource-based economies, one of the first activities to blossom in Indian Country was tobacco retailing. Tribal smoke shops have developed a lucrative business selling cigarettes free of state taxes in defiance of state law.

The Washington State Department of Revenue estimates that in FY 2001 sales by tribal smoke shops represented 15.5 percent of state cigarette consumption, or 64.8 million packs. Of this total, an estimated 56.9 million packs were sold to non-Indians.

The state of Washington currently imposes a cigarette tax of \$1.425 per pack, which is implemented through system of tax stamps. (The rate increased \$0.60, from \$0.825, on January 1, 2002 as a result of Initiative 773.) In addition, cigarettes are subject to state and local sales taxes.

Several U.S. Supreme Court cases involving cigarettes have played a significant role in delineating states' abilities to tax sales occurring on tribal lands. Perhaps the most important of these cigarette cases involved

FIGURE 2
CIGARETTE TAX EVASION ESTIMATE - FY 2001
CIGARETTE TAX 82.5 CENTS PER PACK

The estimates below are determined by comparing WA taxable consumption to US consumption. The data are not detailed enough to quantify enforcement efforts.

Per Capita Estimates:

U.S. Per Capita Consumption	81.1 packs
Washington Per Capita Consumption ¹	69.7 packs
Washington Taxable Consumption ²	49.5 packs
Washington Per Capita Gap Estimate	20.2 packs

Washington Population	6.0 million
Total Washington Loss	120.8 million packs
Less: Legitimate Military Sales ³	(18.1) million packs
Less: Legitimate Indian Sales	(7.9) million packs
Loss from Evasion	94.8 million packs

Revenue Losses:

		\$3.52 Cost Per Pack	
State Revenue Losses:		Tax Per Pack	Revenues
		Cents	Millions
Cigarette Taxes:			
General Fund		23.0	\$21.8
Water Quality		8.0	7.6
Drug Program		10.5	10.0
Health Care		41.0	38.9
		<u>82.5</u>	<u>\$78.2</u>
Other State Excise Taxes:			
Sales Tax	6.5%	22.9	21.7
B&O Tax	0.471%	1.7	1.6
Total		<u>107.0</u>	<u>\$101.5</u>
Local Revenue Loss:			
Local Sales Tax	1.72%	6.1	5.7
Total		<u>113.1</u>	<u>\$107.2</u>

Sources of Evasion:

		Packs	Dollars
Indian Sales	60.0%	56.9	\$64.3
Military Sales	11.0%	10.4	11.8
Casual Smuggling	29.0%	27.5	31.1
Total	<u>100.00%</u>	<u>94.8</u>	<u>\$107.2</u>

¹ Assumes that Washington residents per capita consumption is 86% of the U.S. rate (1997 DOH Study).

² Taxable per capita consumption is based on the actual Fiscal Year 2001 sale of cigarette stamps.

³ Assumes 259,864 military and dependents consuming at the Washington per capita rate of 69.7.

Source: Department of Revenue

the state of Washington: *Washington v. Confederated Tribes of the Colville Indian Reservation*.¹³ In *Colville*, the court held that the burden of the cigarette tax was on the purchaser, and that, while sales to tribal members were exempt, the state's cigarette tax did apply to sales to non-Indians on the Colville reservation.

In explaining this decision, the Court introduced the concept of reservation-generated value (which it elaborated subsequently in *Cabazon*). The on-reservation sale by a tribe or tribal member to a non-Indian is not subject to state taxation when a substantial portion of the good's value derives from on-reservation activity. But a state is allowed to tax a transaction when little value has been added on the reservation, or, as the Court stated succinctly, when the tribal seller is simply "marketing an exemption from state taxation to persons who would normally do their business elsewhere."

Further, the court held that affixing state tax stamps upon packs of cigarettes was a minimal burden and that therefore that the state could impose this requirement on tribal retailers.¹⁴ In spite of the *Colville* decision, however, the state faces a substantial problem in collecting taxes on on-reservation sales because the tribes' sovereign immunity from lawsuits prevents the state from enforcing the obligation to collect and remit taxes.

The court suggested states might enforce their right to tax sales to non-Indians by requiring that off-reservation wholesalers rather than on-reservation retailers collect the tax and by seizing unstamped cigarettes before they are delivered to the tribal lands. Washington has tried both of these approaches, with a notable lack of success.

The Department of Revenue estimates that in FY 2001 Washing-

ton smokers evaded taxes on approximately 23 percent of their cigarette purchases and that as a result state and local government lost \$107 million in revenue. Of this an estimated \$64 million is due to sales on tribal lands. (See Figure 2.)

Recently, the state has thrown in the towel and adopted a new approach to the evasion of taxes on tribal sales. The 2001 Legislature enacted legislation intended “to promote economic development, provide needed revenues for tribal governments and Indian persons, and enhance enforcement of the state’s cigarette tax law, ultimately saving the state money and reducing conflict.”¹⁵

This law allows the governor to negotiate cooperative agreements on cigarette taxation with certain tribes. Under such an agreement, the state exempts sales of cigarettes to non-Indians on the tribe’s lands from state cigarette and sales taxes. In exchange, the tribe would impose its own taxes on cigarette sales at the same rate as the combined state cigarette and sales tax rates. With the tribal taxes in place, on-reservation prices for cigarettes should not undercut the prices offered by off-reservation retailers. This should reduce the incentive for non-Indians to travel to tribal smoke shops and therefore increase the number of sales subject to state taxes.

The Governor is authorized to negotiate contracts with 18 of the state’s 29 recognized tribes. The first contract was signed on December 10, 2001, with the Squaxin Island Tribe. The state subsequently signed contracts with the Tulalip and Upper Skagit Tribes.

The contracts do not block a second, emerging tribal strategy for selling tax-free cigarettes to non-Indians. The Squaxin Island Tribe has established the Skookum Creek Tobacco Company with the intention of manufacturing cigarettes. The enterprise is currently awaiting permits from the Federal Bureau of Alcohol, Tobacco, and Firearms. The Tribe expects that sales of these cigarettes will not be subject to state tax because a significant portion of their value will be reservation-generated.

Tribal Gaming

Large-scale tribal gaming is a relatively new phenomenon. Prior to the mid-1980s, Indian tribes in various part of the country had been operating low-stakes gambling operations in states that did not otherwise allow much in the way of gambling. These consisted mostly of bingo parlors, which attracted primarily non-Indian customers. At the same time that tribes began to realize that these operations could expand to offer different games and be a significant source of revenue, state governments began to get nervous about this loophole in their efforts to prohibit or closely regulate gambling.

Washington State pre-1988

In Washington State, prior to the early 1970s, nearly all forms of gambling (horse racing being the notable exception) had been prohibited. This began to change with a constitutional amendment in 1972. Within a decade, the state had authorized card rooms, “commercial stimulants” such as punchboards and pulltabs, charitable “Reno nights,” sports pools, and, finally, the state lottery. The intent of the original legislation embraces two key goals: avoid criminal activity and support charitable causes:

“It is hereby declared to be the policy of the legislature, recognizing the close relationship between professional gambling and organized crime, to restrain all persons from seeking profit from professional

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gambling activities in this state; to safeguard the public against the evils induced by common gamblers and common gambling houses engaged in professional gambling. . . . The legislature further declares that the raising of funds for the promotion of bona fide charitable or nonprofit organizations is in the public interest as is participation in such activities and social pastimes as are hereinafter in this chapter authorized.”¹⁶

The first large-scale tribal bingo operations began in 1983, with the Tulalips, Puyallups and Muckleshoots opening facilities. The Lummi Tribe attempted to start a blackjack operation, but was shut down by the U.S. Attorney. Meanwhile, the *Cabazon* case was heating up in Southern California.

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The Indian Gaming Regulatory Act

After *Cabazon* set severe limitations on the ability of states to control gambling on tribal lands, Congress realized that there was a significant potential for increased tribal gambling operations. The result was the Indian Gaming Regulatory Act (IGRA), adopted in 1988.¹⁷

The goal of Congress was to establish a federal legal framework that would acknowledge the court-recognized rights of tribes while also acknowledging the interests of the states. The Senate committee report states:

In developing the legislation, the issue has been how best to preserve the right of tribes to self-government while, at the same time, to protect both the tribes and the gaming public from unscrupulous persons.¹⁸

The IGRA, its legislative history, and subsequent attempts to amend it contain several clear statements of policy:

- ❑ Deterring criminal activity. The most frequently mentioned reason for enacting the IGRA was to provide a means to prevent criminal elements from infiltrating tribal gaming operations.
- ❑ Promoting tribal economic development and self-sufficiency. Congress specifically mentions the use of gambling revenues to enhance “skeleton” programs that had been totally dependent on the federal government.
- ❑ Use of revenues. Net revenues from tribal gaming are to be used for tribal operations, “general welfare,” economic development, charitable donations, or to defray costs incurred by local governments. Per capita payments to tribal members are allowed, subject to a plan approved by the Secretary of the Interior.
- ❑ A role for states. *Cabazon* had reaffirmed the minor authority that states have over tribes on non-criminal matters. Congress and the Justice Department, however, recognized that states have a significant interest in the impacts of gaming and are much better equipped than the federal government to regulate high-stakes gaming operations. States would, therefore be given a major role in Indian gaming regulation.

- ❑ Preservation of tribal sovereignty. In granting states this new and unprecedented authority, Congress took pains to circumscribe it, stating explicitly that the authorities given to states under IGRA cannot be construed to extend to any other area of law.
- ❑ Prohibition of taxation. The IGRA states clearly that neither the business operations, the gambling activity itself nor the associated purchases of equipment and services can be taxed by state or local governments.

Tribal-state compacts

The starting point for the IGRA was a recognition of three classes of gaming, each with its own jurisdiction. Most of the action and controversy has been around Class III games.

Under the IGRA, states are required to negotiate in “good faith” with any tribe requesting a state-tribal compact for Class III gaming.

	Types of Games	Jurisdiction
Class I	Social games with very low stakes and winnings	Self-regulated by tribes. Non-Indian intervention
Class II	Bingo, punch cards, pull tabs and some non-	Self-regulated by tribes, with oversight by the
Class III	All games that are not Class I or Class II, including house-banked games, slot machines, racing, lotteries.	Regulated through tribal-state compacts.

Under the IGRA, states are required to negotiate in “good faith” with any tribe requesting a state-tribal compact for Class III gaming. This compact provides the regulatory framework within which tribal enterprises can offer any Class III gambling activities that are in any way permitted within the state, and allows the state to enforce these regulations. The IGRA states that a compact can include provisions for regulation of and jurisdiction over casinos, jurisdiction over civil matters and contracts relating to casino operations, and systems to ensure legal operations.

The IGRA further states that if the state and the tribe cannot reach an agreement, the tribe can file a “bad faith” lawsuit to pursue a mediated settlement, or, as a last resort, the imposition of a compact on the state by the Secretary of the Interior. This provision, however, was thrown out by the Supreme Court, which ruled in the *Seminole* case that the 11th Amendment shields states from being sued in federal court.¹⁹ This ruling invalidated the entire mediation process in the IGRA, leaving tribes without a venue to pursue action against states. The disputes between the Spokane and Colville Tribes and the State of Washington over slot machines have been a direct result of *Seminole*.

Compacts in Washington State

In Washington State, negotiation of compacts is the job of the State Gambling Commission. A designated committee of each house of the Legislature holds a hearing (but does not vote) on a proposed compact. Once the

Commission approves a compact, it is forwarded to the Governor who signs it, along with the tribal chair.

The compacts specify many features, including opening hours (up to 160 per week), wagering limits (\$500), and the number of gaming stations allowed in a facility. Until recently, tribes were allowed one casino location with 50 gaming stations, plus 2 additional non-profit stations whose proceeds are dedicated to support charities.

Recently the state has negotiated revisions to the compacts for the Tulalip, Muckleshoot, and Puyallup Tribes to allow, in each case, two casinos, one with 75 stations and a second with 50 stations. Additionally, the facilities are allowed one non-profit station for every 25 standard stations. To operate more than 60 standard stations, however, a tribe must obtain transfers of unused gaming station authorizations from another tribe.

Since each compact includes a “most favored nations clause,” which provides that the compact should be automatically amended to incorporate any expanded gaming powers granted to any other tribe, all compacted tribes would seem to be allowed the powers granted to the Tulalips, Muckleshoots, and Puyallups.

FIGURE 3
TRIBAL GAMING IN WASHINGTON

Tribe	Location	Compact Date	Operating Casinos
Chehalis Confederated Tribes	Oakville	December, 1992	Lucky Eagle, Rochester
Hoh Tribe	Forks	May, 1995	None
Jamestown S'Klallam Tribe	Sequim	February, 1993	Seven Cedars, Sequim
Kalispel Tribe of Indians	Usk	October, 1998	Northern Quest, Airway Heights
Lower Elwha Klallam	Port Angeles	December, 1992	None
Lummi Nation	Bellingham	September, 1995	Silver Reef, Ferndale
Makah Tribe	Neah Bay	May, 2000	None
Muckleshoot Tribe	Auburn	February, 1993	Muckleshoot, Auburn
Nisqually Tribe	Olympia	May, 1995	Red Wind, Olympia
Nooksack Tribe	Deming	October, 1991	Nooksack River, Deming
Port Gamble S'Klallam Tribe	Kingston	January, 1995	Point No Point, Kingston
Puyallup Tribe of Indians	Fife	May, 1996	Emerald Queen, Tacoma
Quileute Tribe	La Push	July, 1993	None
Quinalt Indian Nation	Taholah	July, 1996	Quinalt Beach Resort, Ocean Shores
Samish Tribe	Anacortes	April, 2000	None
Sauk-Suiattle Tribe	Darrington	April, 2000	None
Skokomish Tribe	Shelton	May, 1995	Lucky Dog, Shelton
Snoqualmie Tribe	Snoqualmie	February, 2002	None
Squaxin Island Tribe	Shelton	July, 1993	Little Creek, Shelton
Stillaguamish Tribe	Arlington	April, 2000	None
Suquamish Tribe	Poulsbo	January, 1995	Clearwater, Suquamish
Swinomish Indian Tribal Community	LaConner	December, 1992	Swinomish, Anacortes
Tulalip Tribes	Marysville	August, 1991	Tulalip, Marysville
Upper Skagit Tribe	Sedro Woolley	December, 1992	Skagit Valley, Bow
Confederated Tribes of the Yakama Indian Nation	Toppenish	June, 1996	Legends, Toppenish
Shoalwater Bay Tribe	Tokeland	Compact pending	Shoalwater Bay, Tokeland
Colville Confederated Tribes	Nespelem	Compact pending	Miller Bay, Manson; Okanogan Bingo, Okanogan; Coulee Dam, Coulee Dam
Spokane Tribe	Wellpinit	No Compact	Two Rivers, Davenport; Double Eagle, Chewelah

Source: Washington State Gambling Commission

The recently negotiated compact with the Colville Tribes allows for three primary gaming facilities and three satellite facilities. The facilities can be no closer than 25 miles from one another.

Most compacts require the tribes to contribute two percent of the net win from Class III games to an impact mitigation fund from which local governments are to be reimbursed for public safety and emergency services costs directly associated with the operation of the gaming facility. If documented impacts do not exhaust the two percent of net win placed in the fund, the tribe may use the balance for other tribal purposes.

So far, 27 tribes in Washington State have concluded compacts for Class III gaming. (See Figure 3.) All compacts now include an Appendix X, which allows the tribe to operate electronic lottery systems (see below). At present, eight tribes with compacts do not operate casinos.

Three tribes have been operating casinos without state compacts, and in each case the primary dispute has been over slot machines. Two of those tribes – Colvilles and Shoalwaters – have recently concluded compacts that will take effect in 2002. The Spokanes are the only tribe continuing to operate casinos without a compact. Only two tribes with current federal recognition have not attempted to negotiate a compact with Washington State.

As evidenced by the size and sophistication of many tribal casinos in the state, Washington's compacts are fairly wide-ranging. At the time the first compacts were being negotiated, Washington law allowed casino-style gambling only in charitable "Reno night" settings. But because of the prohibition/regulatory distinction set forth in *Cabazon*, those games could be offered in tribal facilities at any level under any Class III compact.

Slots and lotteries

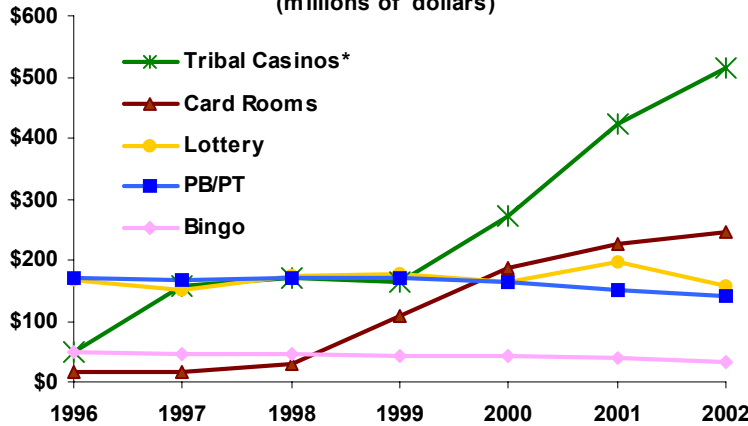
Slot machines have never been allowed under any circumstances in Washington State, and therefore could be banned from tribal casinos under the *Cabazon* logic. Because of their high revenue generation and low labor intensity, slots are popular with casino operators, and several tribes have attempted to introduce them over the years, asserting that the state's refusal to allow them constitutes bad faith. In a pair of unsuccessful efforts to get around adverse court rulings on slot machines, tribes in the state promoted ballot initiatives to allow them, first in 1995 and again in 1996.

In 1994, in an attempt to bring some final resolution to the question of slot machines, the state agreed to a limited waiver of its 11th Amendment immunity from lawsuit, and to be subject to a "friendly lawsuit" that would allow a federal court to resolve the issue. In September 1997, the court confirmed the state's position that tribal casinos could not have stand-alone slot machines.

At the same time, the court determined that tribes could offer "electronic lottery systems." Unlike slot machines which operate as fully independent devices, lottery machines are all connected to a central computer that pre-determines winners. To the player these may seem like slot machines (and they are often advertised as such), especially since the terminals are designed to look similar and provide a similar experience. Mathematically, however, they are a lottery: the player is not playing against a machine, but against other patrons of the casino who are playing on other machines

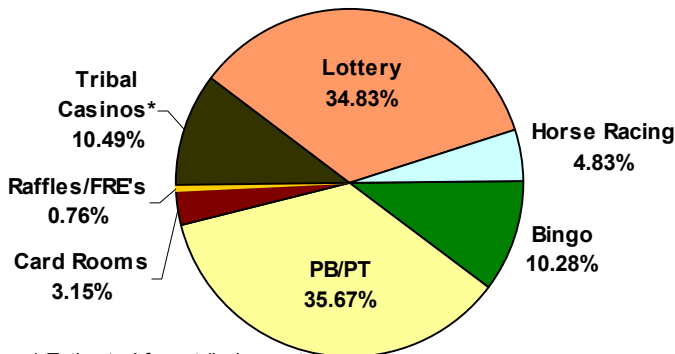
As evidenced by the size and sophistication of many tribal casinos in the state, Washington's compacts are fairly wide-ranging.

FIGURE 4
Net Revenues from Various Gambling Activities
 (millions of dollars)



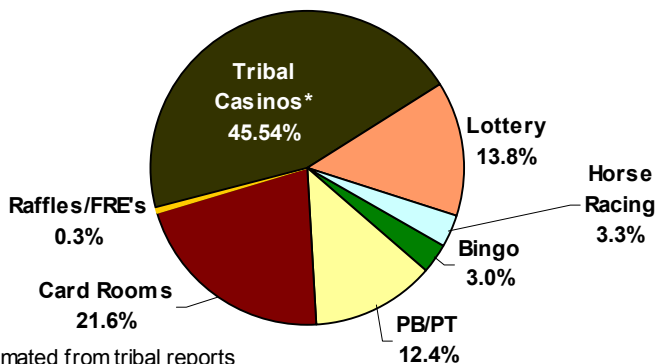
* Estimated from tribal reports
 Source: Washington State Gambling Commission

FIGURE 5
Gambling in 1996
 (\$477 million)



* Estimated from tribal reports
 Source: Washington State Gambling Commission

FIGURE 6
Gambling in 2002
 (\$1,130 million)



* Estimated from tribal reports
 Source: Washington State Gambling Commission

connected to the same central computer, with all players hoping to get one of the pre-determined winning instant lottery “tickets.”

Additionally, these machines cannot have levers or spinning dials. And, instead of using cash or coins, they must use pre-paid smart-cards and provide a print-out of winnings. Tribal casinos can also produce their own scratch lottery tickets, provided that they too have computer-generated outcomes.

Each tribe with an existing compact could negotiate an Appendix X and be allocated terminals (425 at first, going up to 675). Tribes that do not operate casinos, or which cannot use all of their allocation, can lease their allocation to other tribes. The income from leasing lottery terminal allocations is the primary reason several tribes entered into compacts with no intention of opening casinos. The cap for any facility is 1,500 terminals. (The Colville Tribes are allowed to operate a maximum of 4,800 terminals, with no more than 2,000 terminals at any primary facility and no more than 100 terminals at any satellite facility.) Currently, there are over 9,000 terminals in operation across the state.

Growth of Gambling

Gambling activities of all kinds have grown substantially in the past decade in Washington, and have more than doubled since 1996. During that time, tribal casinos have gone from an almost negligible position in the market to its dominant player.

A useful measure of the magnitude of gambling activity is “net receipts,” which equals the amount wagered by gambling patrons less the amount paid out in prizes. Figure 4 shows the growth of various gambling activities since 1996. While most gambling activities have been relatively flat over this period,

casinos, both tribal and non-tribal, have grown substantially. The major acceleration of tribal casino revenue corresponds with the introduction of lottery machines. In just two years, tribal casino net receipts increased 217 percent.

The substantial increase in revenue from card rooms in over the past few years has been a result of legislation that allowed house-banked card games. Prior to 1997, card rooms could only offer games in which players wagered against each other. With house-banked games players wager against the casino, allowing for a wider variety of games and an atmosphere friendlier to the casual gambler. These new mini casinos are allowed 15 tables but cannot offer the electronic lottery games that have become so popular at tribal casinos.

Figures 5 and 6 show how the state’s gambling market is split. Tribal casinos generated 10 percent of all gambling revenue in 1996, and by 2002 were generating nearly 46 percent.

As was earlier noted, providing revenue for charitable and nonprofit organizations was the legislature’s original purpose in it authorizing gambling in the state. The growth in casino gambling has had a significant impact on these organizations. In fiscal year 1996, charity and nonprofit net receipts from gaming totaled \$88.6 million. By FY 2002 their net receipts fell by 35 percent, to \$57.2 million. In six years, spending on these games has fallen from 19 percent of all gambling in the state to 5 percent. (See Figure 7.)

Gambling taxes

Across the country, as gambling has grown, state and local governments have recognized its tax revenue potential, and have imposed heavy taxes on non-tribal gambling. The IGRA specifically prohibits states from taxing not only the casino operations, but also non-tribal businesses that operate gambling businesses on behalf of tribes or that supply casinos with goods and services.

In Washington State, state and local governments are specifically prohibited from taxing any aspect of tribal gaming, whether it is business and occupation tax on operations, or sales and use taxes for equipment. And, of course, there are no taxes on gambling itself.

The tribes do make impact mitigation payments to local governments for demonstrated costs borne by them as a result of gaming operations on adjacent tribal lands. The reimbursement is generally capped at two percent of net revenues from Class III gaming. A July 2002 report for the tribally-funded First American Education Project provides information on how these moneys have been distributed. For the years 1993 through 2001, tribes have reported to the Washington State Gambling Commission that they distributed

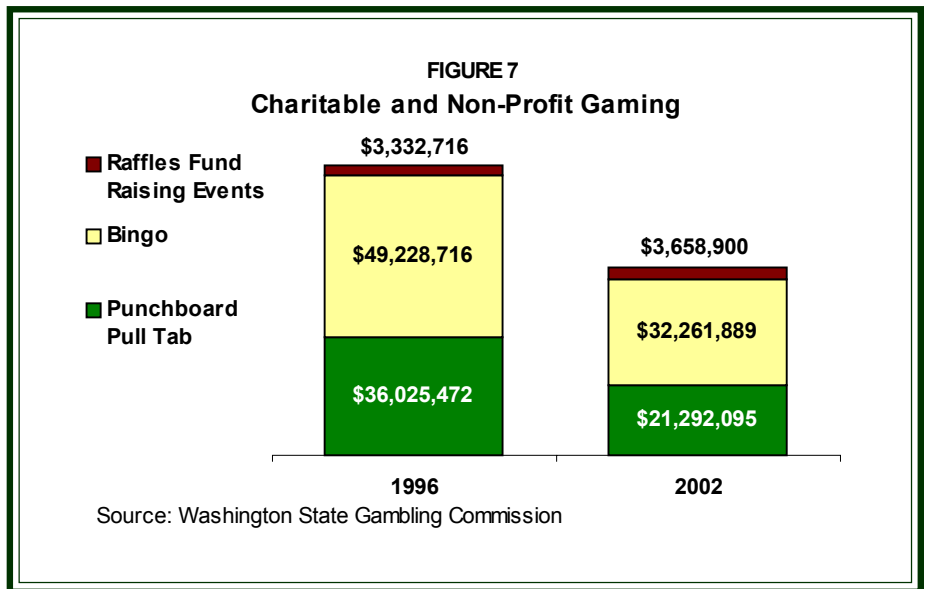
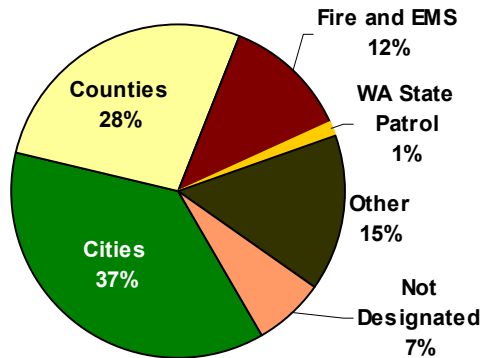
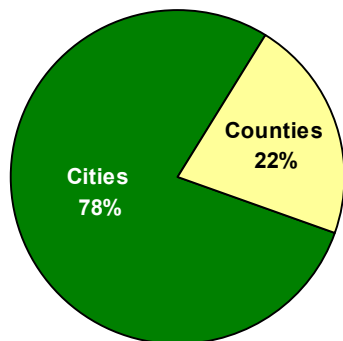


FIGURE 8
Two Percent Payments Reported by Tribes 1993-2001
\$16.9 million



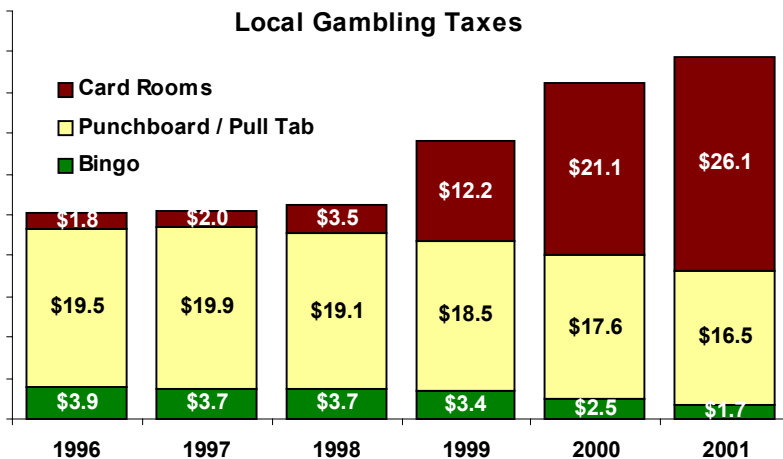
Source: First American Education Project

FIGURE 9
Local Gambling Taxes 1993-2001
\$298.7 million



Source: State Auditor

FIGURE 10
Local Gambling Taxes



Source: Washington State Gambling Commission

\$17 million in impact mitigation payments. (This may understate the payments actually made. Though, by the terms of their compacts with the state, tribes are required to report these distributions to the Commission, the authors of First American Education Project report believe that the data for 2000 and 2001 are incomplete.) Of the reported \$17 million in distributions, 37 percent, \$6.3 million, went to cities; 28 percent, \$4.7 million, went to counties. (See Figure 8.)

In contrast, non-tribal card rooms and mini-casinos are subject to the full array of business taxes: sales tax on food and beverages, business and occupation tax, sales tax on construction and equipment purchases, etc. Additionally, local governments can levy a tax of up to 20 percent on gross receipts from gambling (this is defined as the house's win after collecting all losing wagers and paying winners). Actual rates range from five to twenty percent, with over half of jurisdictions with cardrooms setting their rates at 10 or 11 percent.

From 1993 through 2001, Washington cities and counties received \$298.7 million in gambling taxes from card rooms, bingo, punchboards, pull tabs, and other gaming activities. The greater part of this, \$233.8 million went to cities. (See Figure 9.)

Figure 10 shows the sources of gambling taxes collected by local governments from 1996 through 2002. Revenues have grown from \$25.2 million in 1996 to \$44.3 million in 2002. This growth was the result of the introduction of house-banked gaming at the card rooms. Taxes from punch boards, pull tabs and bingo declined over the period.

The cities of Auburn and Kent are near to the Muckleshoot casino. Auburn has a card room, Freddie's Club, which opened in 1998. The

city's gambling tax receipts grew from \$225,000 in 1996 to \$1,059,000 in 2001. In contrast, without a card room, Kent's gambling taxes fell from \$489,000 to \$312,000 over the same period.

Current Issues

While Indian gaming remains controversial, most of the action has been taking place in the federal court system and in federal regulatory decisions. Few pieces of legislation at either the federal or state level have been adopted in recent years. Current issues include:

Expansion of non-tribal gaming. In response to the rapid growth of tribal casinos, the 1997 legislature authorized non-tribal cardrooms to offer house-banked card games. This substantially increased card rooms' popularity and revenue. It also substantially increased local governments gambling tax receipts. Between 1996 and 2001, local gambling tax revenues increased by 76 percent, to \$42.3 million. A dramatic increase in taxes from card rooms offset declines in bingo, punchboard and pull tab taxes.

The introduction of lottery machines in tribal casinos, however, once again put non-tribal cardrooms at a disadvantage. Card room, bingo, tavern and restaurant operators are now seeking legislative authorization to operate lottery machines. While such a move remains controversial, the potential tax revenue to state and local governments would be attractive.

Role of state legislatures in compacts. Currently, tribal-state compacts are negotiated and approved exclusively by the executive branch of state government, with the legislature's role confined to a single public hearing. There have been efforts at the federal level (HR 2244, introduced in June, 2001) and in Washington State (SB 5265, 1997-1998 session) to provide a role for state legislatures. None have been successful thus far.

State sovereignty. A central flaw in the compacting process of the IGRA remains the issue of state sovereignty under the 11th Amendment which can create an impasse between states and tribes. Recent Washington State legislation allows for a limited waiver of immunity by the state to allow a federal court to resolve disputes with compacted tribes. It does not, however, provide for a waiver in a case involving the remaining non-compacted tribes, including the Spokanes.

Ability of Secretary to implement compacts. In 1999, to get around the 11th Amendment problem, the Interior Department adopted a process that would allow the Secretary to implement the equivalent of a gaming compact without a state's consent.²⁰ The states objected strongly, and the process has been put on hold, pending the outcome of a lawsuit filed by the states of Florida and Alabama.

Benefits to contractors. Congress specifically stated that the great majority of financial gain from tribal gaming should accrue to the tribes themselves. Because tribal gaming operations buy or lease nearly all their equipment from outside vendors, and use a variety of outside services, allegations have arisen about excessive benefits accruing to these contractors.

Trust Lands. The federal government can take into trust lands, not necessarily adjacent to a reservation, for use by tribes. This process is often used to provide land to newly-recognized tribes. It can also be used to expand existing tribal holdings for housing and, under certain circumstances, gaming facilities. In 1999 the Interior Department proposed a new process

for taking land into trust. The rule was published in the last days of the Clinton Administration, and was subsequently frozen by the Bush Administration, along with other last-minute regulations. The states strongly objected to the process, and it has since been withdrawn.²¹

Each trust land expansion provides new opportunities for tribal economic activity outside of the state's tax and regulatory system.

In 1996 the federal government took land at Airway Heights, near Spokane, into trust for the Kalispel Tribe. In 2000 the Tribe opened the Northern Quest Casino on this land. It further plans to open a business park, Kalispel Commerce Park, at this site.

Each trust land expansion provides new opportunities for tribal economic activity outside of the state's tax and regulatory system.

The newly-recognized Snoqualmie Tribe wants the federal government to bring 56 acres into trust for the Tribe outside King County's urban growth boundary along I-90 near to North Bend. On the land, the Tribe plans to develop a casino, theatre, three restaurants, and a 900-car parking lot.

The Cowlitz Tribe owns a 152-acre plot of land near I-5 at La Center. The Bureau of Indian Affairs is considering the Tribe's request that this land become trust land. While the Tribe says that as yet it has no definite plans as to how the site will be developed, it is known that the Tribe has explored the possibility of building a casino. La Center is the home of a cluster of four card rooms, including two that are among the top ten in the state in net receipts.

The Chehalis Tribe operates a successful casino, the Lucky Eagle, on its reservation in Rochester. The Tribe is investigating building a new casino-hotel complex off of the current reservation near I-5 in Grand Mound.

Recent Non-Gaming Tribal Business Development

Several tribes have leveraged the success of their gaming operations to branch out into other businesses that they believe have good prospects for the long term. Following are some examples.

White River Amphitheater

In 1997 the Muckleshoot Tribe began work on a 23,000-seat outdoor concert venue overlooking the White River between Auburn and Enumclaw. The facility would be booked and managed by a national promotion company, and would provide a venue similar to the Gorge amphitheater in George Washington.

A principal advantage of the White River location would be its close proximity to the large customer base of the Puget Sound area. Because of the need for long drives and/or camping, the Gorge tends to focus on a somewhat younger audience, leaving the older, less adventurous audiences available for a facility closer to home. Additionally, unlike the Gorge, White River would have half its seats under a canopy.

The Tribe began construction, but it was halted in 1998 by a series of court actions seeking either to stop the project entirely or require major mitigation of traffic and other impacts. The project is outside the urban growth boundary, raising concerns about the spread of development into rural areas. Opponents, however, failed to make much headway in the face of claims of tribal sovereignty, and the project will need only two permits from outside governments: an Army Corps of Engineers permit to fill a wetland, and a Washington State DOT permit to tie into a state highway.

Since construction first began, the Tribe has scaled back the project somewhat to 20,000 seats. The facility will provide parking for 6,500 vehicles on-site, and contract with the Supermall in Auburn for an additional 800 parking spaces, with shuttle service. The project will also include a restaurant with seating for 700 people as well as 100 points of sale around the complex.

The tax situation at the amphitheater will be mixed. Ticket sales occurring off the reservation should be taxable, as should on-site merchandise sales to non-tribal members. On-site operations of Clear Channel Entertainment may be taxable, but operations conducted by the Tribe would not be. If there is sufficient value-added in the food and beverage service, it should not be taxable. Since the state has limited ability to enforce collection of taxes by tribal operations, a collection system will have to be negotiated.

Quil Ceda Village

A major determinant of tribal success in businesses has been proximity to major population centers and freeways. The Tulalip reservation in Snohomish County enjoys both advantages, being just north of Everett and next to the booming city of Marysville, as well as immediately adjacent to Interstate 5. The retail, commercial, and industrial complex known as Quil Ceda Village takes full advantage of this key location.

The 2,000-acre complex, just west of I-5 and north of the existing Tulalip casino, currently has a Wal-Mart and a Home Depot, both of which opened in 2001. A new larger casino is now under construction, and a hotel and conference center are planned for the same area. Also getting underway is a 30,000 square foot Neighborhood Town Center, which will house smaller businesses and services. By 2020, it is projected that businesses at the complex will employ 6,500 workers in addition to the 1,300 employed at the casino.²²

As the development took shape, the Tribe attempted to capture all of the sales tax receipts collected on site. They incorporated the area as a city – the first tribal city in Washington – and asked Wal-Mart and Home Depot to remit all sales taxes to the new city. The state objected to this strategy, and both retailers sent their tax collections to the state. The state Department of Revenue asserted that although tribes can levy taxes in addition to those collected by the state, they couldn't do so in lieu of state taxes. Legislation has been drafted to allow tribes to share in sales tax collections, but it has not passed the legislature.

Since the sales tax is levied on the customer, not the store, non-tribal customers would be liable for taxes on purchases made on tribal lands. Non-tribal businesses would be liable for sales tax on construction of buildings on the reservation. Under the IGRA, however, the new casino would not be liable for sales tax on construction.

An economic impact study prepared for the city of Marysville projects that the development could cost the city \$60 million (constant 2002 dollars) between 2003 and 2020 in lost tax revenue and increased service costs.²³

As the impact study explains, Marysville is currently a bedroom community for Everett and Seattle. People who live in Marysville tend to work and shop outside of the city limits, and the city suffers from “revenue leakage”. As regional population grows, commercial and retail development within the city would ordinarily be expected to reduce the leakage. However,

As the development took shape, the Tribe attempted to capture all of the sales tax receipts collected on site. They incorporated the area as a city – the first tribal city in Washington – and asked Wal-Mart and Home Depot to remit all sales taxes to the new city.

tax and regulatory advantages will draw much of this development to Quil Ceda Village.

The competition with Quil Ceda Village for business and sales tax revenue has spurred the City of Marysville to take a hard look at the business and development climate in the city. The City launched a study of how to attract and retain businesses, and has overhauled its permitting and inspection processes to make the city more attractive to developers.

Puyallup casino complex

The Puyallup Tribe already has one of the most successful casinos in the state – the Emerald Queen – and is now planning to build the largest, along with a hotel, entertainment complex, retail area, restaurants and health spas. The \$200-million project will be next to Interstate 5 on Tacoma's East Side, where demolition has already begun. The existing tribal headquarters will be moved to a site in Fife.

Although plans are not final, they call for a 250-room hotel, five restaurants, a 3,500-seat performance auditorium, and numerous water features. The complex, as envisioned, would go far beyond the current stand-alone casinos and emulate the larger complexes in Nevada. The 94,000 square-foot casino floor is comparable to several casinos in Reno.

Concerts and shows at the Tribe's new performance auditorium will avoid the City of Tacoma's 5 percent admissions tax; events at the Emerald Queen Casino currently do.

Overnight guests at tribally owned hotels escape the sales tax imposed at nearby non-tribal hotels. This can be a substantial competitive advantage. In Tacoma, in addition to the standard 8.8 percent sales tax, hotel patrons pay a special hotel-motel tax of 5 percent. Near Quil Ceda, a 2 percent special hotel-motel tax is added to the standard 8.5 percent sales tax.

Avoidance of the 13.8 percent tax will represent a major cost advantage for the Puyallup's hotel as it competes with nearby non-tribal hotels. Were the tribal hotel to divert an average of 100 patrons a night at \$100 per room from other local hotels, the annual loss of revenue to the state and local governments would be just over \$500,000.

Both the Puyallup and Tulalip projects include plans for major conference and event facilities, causing concern in communities where similar publicly-funded projects are in the works. Several cities, recognizing the need for new mid-sized conference facilities outside of the Seattle-SeaTac-Bellevue triangle, have sought to get into this potentially lucrative business. The tribal facilities, because they are connected to casinos, would seem to have a competitive advantage. They would have tax advantages on value-added services, and if owned by tribes, the facilities would not be liable for sales tax on construction. With this looming competition, some local jurisdictions are reevaluating their plans.

Energy projects. A number of tribes in the West are exploring possibilities in the energy business.

The Makah Tribe is working with a private business to construct an electric generating facility using the energy of ocean waves. A series of offshore buoys would generate electricity and transmit it through cables to the coast. The power would be sold to the Clallam County PUD.

A Night Out: A Taxing Experience?

Jane Smith, Kirkland resident, receives a bonus of \$150. She decides to spend the windfall on a night out with her husband. They go to dinner at a Seattle Jazz club, spending \$20 for a cover charge and \$130 for drinks and dinner (taxes included). The following is the tax revenue that results.

Admissions tax	\$0.95
State sales tax	\$7.73
Local sales taxes	\$2.74
Food & beverage tax	\$0.59
State B&O tax	\$0.85
City B&O	\$0.33
Liquor taxes	\$1.00
Total taxes	\$14.19
Net to club	\$135.81

The total taxes exceed 10 percent of the net to the club. Avoiding this "wedge" is a competitive advantage for tribal casino/entertainment complexes like the one planned by the Puyallups.

The Colville Tribes recently purchased and reopened a wood products mill that has a co-generation plant. The plant is capable of generating 7.5 megawatts of power, which is used to operate the plant and light the Tribe's casino. The Tribe aims to sell surplus power to the Okanogan PUD.

All of these energy projects take advantage of the Tribes' exemption from stringent state regulations on energy facilities. Projects on tribal land would be subject to federal approvals, but would not have to go through the protracted processes of the state's Energy Facilities Site Evaluation Council (EFSEC). Recent experiences of utilities attempting to site generation plants point to the benefits of locating energy facilities on tribal lands.

The Yakama Tribe has been attempting to form its own utility to distribute electricity to customers on the reservation who are currently served by PacifiCorp. The Tribe has an agreement with the Bonneville Power Administration to supply electricity, and has designs on obtaining PacifiCorp's distribution network. The Tribe had earlier considered a joint bid with PacifiCorp to obtain the Grant County PUD's Priest Rapids and Wanapum Dams on the Columbia, which are up for relicensing.

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Observations and Conclusions

The overall legal and regulatory environment within which tribes operate their businesses is well established. Congress could make some changes in the government-to-government relationship between the tribes and the federal government, but much of the relationship is defined in various treaties that cannot be changed unilaterally.

Within a relatively stable overall framework of regulation and taxes, however, much ambiguity remains at the margins, and cases will continue to come before courts. Because the preemption tests used to determine state or federal jurisdiction are fact based, courts will continue having to resolve cases as the myriad variations of conflict come before them.

State and local governments have little direct authority in Indian Country. The federal government expressly grants state governments some authority in areas of regulation where they clearly have a superior administrative capability. States also have taken on some authorities in the absence of any federal preemption, but these cases are very recent.

Under the authority of the Indian Gaming Regulatory Act, tribes are opening major casinos that offer a range of gaming experiences not available at non-Indian establishments.

Although some Members of Congress disapprove of the spread of gambling throughout Indian Country, any attempts to impose significant restrictions would encounter major legal obstacles. State and local governments that disapprove of the trend in gaming have almost no means of restricting tribal gaming as long as gaming is allowed under any circumstances within their borders.

Tribal gaming maintains sufficient support among political leadership to make new restrictions unlikely in the near future. Barring some major scandal, tribal gaming is likely to continue in its current form for some time to come. Any reduction in gaming activity will more likely be a result of changes in the market for that kind of entertainment.

As the state has tried to level the competitive playing field between tribal and non-tribal gambling operations, the only option available is to increase the permissible level of activity in non-tribal gaming businesses. The first ratcheting up of cardrooms occurred with the expansion of tables in 1996 and then authorization of house-banking in 1997. The introduction of lottery machines in tribal casinos once again tilted the competitive field toward tribal casinos, bringing pressure to allow the machines in mini-casinos. Future plans for new and larger tribal casinos will likely be followed by requests to allow further expansion of non-tribal operations.

The Tulalips, Muckleshoots, and Puyllaps are using casino profits to expand into other lines of business. Tribal businesses operate with regulatory and cost advantages over non-tribal businesses. Although these benefits are difficult to quantify, they provide a noticeable advantage to the tribes.

The successful models of non-gaming businesses begun by tribes involve partnerships with large, well-capitalized non-tribal entities.

State and local governments have limited ability to collect taxes from activities on tribal lands. Money spent at non-taxed tribal businesses would, in the absence of those businesses, be spent at taxable businesses, generating state and local government revenue. The amount of foregone revenue is not trivial. Cities such as Marysville and Tacoma have seen activity drawn away from their downtown cores to tax free suburbs.

The successful models of non-gaming businesses begun by tribes involve partnerships with large, well-capitalized non-tribal entities. Outside businesses and investors can take advantage of good locations, available sites and a friendly regulatory climate on tribal lands. For example, it is very unlikely that Clear Channel Entertainment, a large national company that will operate the White River Amphitheater, could have developed such a facility on non-tribal lands without significant legal obstacles and public opposition. When Home Depot or Wal-Mart went looking for a site around Marysville, they saw distinct advantages in being part of Quil Ceda Village.

As growth management continues to restrict the availability of industrial land, some tribes will find themselves in possession of a valuable and increasingly scarce commodity: developable property free of state and local regulations.

(Endnotes)

¹ 18 USC 1151

² Cherokee Nation v. Georgia, 30 U.S. (5 Pet.) 1, 17 (1831)

³ Montana v. United States, 450 U.S. 544 (1981)

⁴ California v. Cabazon Band of Mission Indians, 480 U.S. 202 (1987)

⁵ Ibid.

⁶ Ibid.

⁷ Ibid.

⁸ Keri Murakami, "Getting There: The reasons why we have left-hand onramps," *Seattle Post Intelligencer*, Oct. 21, 2002.

⁹ The Indian Tribal Government Unemployment Compensation Act Tax Relief Amendments, which were part of the Consolidated Appropriations Act for 2001.

¹⁰ SSB 6007

¹¹ Federal Power Commission v. Tuscarora Indian Nation, 362 U.S. 99 (1960)

- ¹² Donovan v. Coeur d'Alene Tribal Farm, 751 F.2d 1113 (9th Cir. 1985)
- ¹³ Washington v. Confederated Tribes of the Colville Indian Reservation, 447 U.S. 134 (1980).
- ¹⁴ See also *Moe v. Confederated Salish and Kootenai Tribes*, 425 U.S. 463 (1976).
- ¹⁵ ESSB 5372
- ¹⁶ RCW 9.46.010
- ¹⁷ Indian Gaming Regulatory Act. 25 U.S. Code section 2710
- ¹⁸ S. Rept. 100-446, 2d session, 1988
- ¹⁹ *Seminole Tribe of Florida v. State of Florida*, 517 U.S. 1133 (1996)
- ²⁰ 25 CFR Part 291
- ²¹ Federal Register: November 9, 2001, Volume 66, Number 218, Page 56608-56610
- ²² Gardner Johnson, *The Economic and Fiscal Impacts arising from the Development of Quil Ceda Village, Marysville, Washington State*, Prepared for the City of Marysville, Seattle, Gardner Johnson, May 2002, Exhibits 3 and 6..
- ²³ *Ibid.* Exhibit 15.

