TAXATION OF BUSINESSES IN INDIAN COUNTRY

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I. STATE TAXES

A. BASIC CONCEPTS.

1. Tribal Sovereignty. In *Worcester v. Georgia*, 31 U.S. (5 Pet.) 515, 561 (1832), Chief Justice John Marshall held that:

> [T]he Cherokee nation . . . is a distinct community, occupying its own territory, with boundaries accurately described, in which the laws of Georgia can have no force, and which the citizens of Georgia have no right to enter but with the consent of the Cherokees themselves or in conformity with treaties and with the acts of Congress.

In *Oliphant v. Suquamish Indian Tribe*, 435 U.S. 191 (1978), the Supreme Court said that Indian tribes retain all the powers of sovereign nations except (1) those taken away by treaties

and agreements, (2) those which have been expressly taken from them by federal statutes and regulations and (3) those which are inconsistent with their "dependent status."

2. The "Infringement" Test: *Williams v. Lee*, 358 U.S. 217 (1959). There are now two independent legal barriers to the application of state laws within Indian Reservations. The first stems from *Williams*, in which the Supreme Court said that the concept of tribal sovereignty expressed in *Worcester v. Georgia* had been modified over the years; that is, states were no longer totally barred from exercising their jurisdiction on Indian reservations. However, the Court laid down the test of whether state law applies inside a reservation as follows: "Essentially, absent governing Act of Congress, the question has always been whether the state action infringed on the right of reservation Indians to make their own laws and to be ruled by them." *Williams*, 358 U.S. at 220.

By 1982 this doctrine was developed into a full-blown "infringement test" which constitutes the first of two "barriers" to the application of state law to non-Indian activities on Indian reservations.

3. The Federal Preemption Test: *Warren Trading Post Co. v. Arizona State Tax Comm'n*, 380 U.S. 685 (1965). The second legal barrier to the application of state laws within Indian reservations stems from *Warren*, in which the Supreme Court held that when the federal government regulates an area of activity so completely that there is no room left for state regulation, the federal government has preempted the area and displaced state law from it. In *Warren*, the Supreme Court held that Arizona could not impose a transaction privilege tax on a federally-licensed Indian trader doing business with reservation Indians on an Indian reservation because the tax intruded into the area of federal licensing and regulation of Indian traders on reservations. This doctrine of federal preemption has developed into a full-blown "preemption test," designated by the Supreme Court as the second of the two "barriers" to the application of state law to non-Indian activities on Indian reservations.

Federal preemption flows from the Supremacy and Commerce Clauses of the United States Constitution. But federal preemption in Indian law is strikingly different from the doctrine of federal preemption in other areas of the law. Because of the tradition of Indian sovereignty over the reservation and tribal members, federal preemption in Indian law does not require an *express* congressional statement that state law has been preempted, as it does in non-Indian cases. All it requires is the finding of a congressional purpose of promoting tribal independence and economic development in relevant federal statutes. *Ramah Navajo School Board, Inc. v. New Mexico Bureau of Revenue*, 458 U.S. 832 (1982).

Within the limits described above, the Supreme Court has held that an Indian tribe retains (1) sovereignty over its members, and (2) sovereignty over its territory.

4. Delegation. In *United States v. Mazurie*, 419 U.S. 544 (1975), the Supreme Court upheld a tribal law which regulated liquor distribution and use on a Reservation. The authority to enact the tribal law had been *delegated* to the Tribe by Congress which itself had the power to regulate reservation liquor sales. The Court said that is was easier to sustain the delegation because the Tribe had "a certain degree of independent authority over matters that affect the internal and

social relations of tribal life." *Id*. at 557.

5. Tribal Preemption. The concept of tribal preemption grows out of the idea of tribal sovereignty. When a tribe, exercising its inherent governmental authority, has enacted a regulatory or tax law, and the state has enacted a law in conflict with it, the tribal law may preempt the state law; that is, it should bar its application on the reservation.

6. Indian Commerce Clause. The United States Constitution, Art. I, § 8, cl. 3, gives Congress the power, "[t]o regulate Commerce with Foreign nations and among the Several states, *and with the Indian Tribes*." In *Washington v. Confederated Tribes of the Colville Reservation*, 477 U.S. 134 (1980), the Supreme Court *suggested* that the Indian Commerce Clause might have a "role to play in preventing undue discrimination against, or burdens on, Indian commerce." *Id*. at 157. The Court indicated that undue discrimination or burdens might occur where state taxes are imposed upon "commerce that would exist on the reservations without respect to" tax exemptions. *Id*. In *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130 (1982), the Supreme Court stated that the Indian Commerce Clause alone might invalidate a state tax on commercial activity inside a reservation in the event the tax was more than would be justified by the state's contact with the activity.

7. Public Law 83-280. The Supreme Court has said in *Bryan v. Itasca County*, 426 U.S. 373 (1980), discussed below that this law, which conferred on certain states civil or criminal jurisdiction over reservation Indians, did *not* confer authority on those states to tax the property of reservation Indians.

B. INFRINGEMENT TEST.

1. *Williams v. Lee*, 358 U.S. 217 (1959). The *Williams* case grew out of commercial transactions between Paul and Lorena Williams, enrolled members of the Navajo Nation, and Hugh Lee, a non-Indian who operated the Ganado Trading Post within the Navajo Reservation. The Williamses bought supplies from Lee on credit and when they failed to pay their bill, Lee brought suit in the Arizona Superior Court. The Williamses filed a motion to dismiss on the ground that only the Tribal Court had jurisdiction over them, but the state court dismissed the motion and awarded Lee a judgment against them.

The matter was upheld in the Arizona Supreme Court, but on appeal to the United States Supreme Court the case was reversed. The Supreme Court pointed out that the Navajo treaty provided that internal affairs of the Tribe would remain exclusively within the jurisdiction of the Tribe and noted that the government had steadily strengthened the tribal government and the tribal courts. Adding that the Navajo Tribal Court had specific jurisdiction over suits by outsiders against tribal members, the Supreme Court concluded, 358 U.S. at 223, that

There can be no doubt that to allow the exercise of state jurisdiction here would undermine the authority of the tribal courts over Reservation affairs and hence would infringe on the right of the Indians to govern themselves.

2. Analyzing Infringement. The Supreme Court's conclusion is easily justified by a simple example: suppose that the Williamses sued Lee in Tribal Court for selling them shoddy merchandise and obtained a Tribal Court judgment canceling their debt to Lee and awarding them an additional amount for damages. But imagine that at the same time Lee obtained a money judgment against the Williamses in the Arizona Superior Court for their failure to pay their debt. Which judgment would be proper? Or enforceable? It would obviously make no sense for the Tribal Court to seize Lee's merchandise at the Trading Post to satisfy the Williamses' judgment at the same time the Arizona Superior Court allowed Lee to seize the Williamses' automobile on the Reservation or to garnish the bank account of the Williamses off the Reservation to satisfy Lee's judgment. Such a result would obviously damage the Tribal Court's authority and make a mockery of tribal judicial proceedings. The Supreme Court's use of the term "infringe" quickly resulted in usage of the term "the infringement test."

C. FEDERAL PREEMPTION TEST.

1. *Warren Trading Post Co. v. Arizona State Tax Comm'n*, 380 U.S. 638 (1965). The second legal barrier to the application of state law to Indian Reservations also derived from a case involving the Navajo Indian Reservation and involved transactions at another trading post. *Warren* grew out of commercial transactions between enrolled members of the Navajo Nation and the operator of the Warren Trading Post within the Navajo Reservation. Arizona levied its 2% gross sales tax on retail sales to tribal members made pursuant to a federal trader's license granted to Warren by the Commissioner of Indian Affairs under the federal trader statutes.

Warren's challenge to the tax on the grounds that it (1) violated art. I, § 8, cl. 3 of the United States Constitution, which provides that "Congress shall have Power...To regulate Commerce...with the Indian Tribes", and (2) was inconsistent with the comprehensive congressional plan regulating federal Indian traders, was overruled by the Arizona Supreme Court; but again the United States Supreme Court reversed the case. The Supreme Court began by noting that the Reservation was set apart as a "permanent home" for the Navajo Nation in their treaty in 1868 and that from the very beginning of our federal government, Indians have been permitted to govern themselves free from state interference.

The Supreme Court underscored that through statutes and treaties, the federal government has exercised a sweeping and dominant control over federal Indian traders. The Supreme Court enumerated federal statutory restrictions on such traders, such as the kind of goods sold, prices which could be charged of Indians, required licensing procedures for Indian traders, penalties for license violations, recordkeeping, bond requirements, and provisions authorizing tribal taxes.

The Supreme Court then held, 380 U.S. at 690-91:

These apparently all-inclusive regulations and the statutes authorizing them would seem in themselves sufficient to show that Congress has taken the business of Indian trading on reservations so fully in hand that no room remains for state laws imposing additional burdens upon traders.

. . . .

. . . the assessment and collection of this tax would to a substantial extent frustrate the evident congressional purpose of ensuring that no burden shall be imposed upon Indian traders for trading with Indians on reservations except as authorized by Acts of Congress or by valid regulations promulgated under those Acts. This state tax on gross income would put financial burdens on appellant or the Indians with whom it deals in addition to those Congress or the tribes have prescribed, and could thereby disturb and disarrange the statutory plan Congress has set up in order to protect Indians from prices deemed unfair or unreasonable by the Indian Commissioner.

2. *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980). In the 1960s, the White Mountain Apache Tribe decided to organize the Fort Apache Timber Company (FATCO) as a wholly-owned tribal enterprise to operate a tribal sawmill in order to maximize tribal profit from its vast timber resource and at the same time provide jobs and training to tribal members. But in doing so, the Tribe concluded that it would be most economical for the Tribe to contract the logging operations to Pinetop Logging Company, a non-Indian enterprise organized solely for the purpose of conducting tribal logging operations on the reservation. In that way, the Tribe could avoid the immense investment required to obtain heavy-logging equipment and could concentrate its limited resources on acquiring the sawmill itself.

After operations began, Arizona attempted to impose upon *all* of Pinetop's activities inside the reservation upon state highways, Bureau of Indian Affairs and tribal roads alike, a 2.5% motor carrier license tax and a use fuel tax of eight cents per gallon for use of the state public highways. Pinetop and the Tribe challenged the taxes under federal law, but wisely chose to limit the challenge to Pinetop's use of Bureau of Indian Affairs and tribal roads. The Arizona courts concluded that the federal interest in regulating tribal timber was not so dominant as to preclude the state taxes and upheld them.

But the United States Supreme Court reversed the case and struck down the state taxes. The Court first noted that:

Congress has broad power to regulate tribal affairs under the Indian Commerce Clause, art I, § 8, cl. 3. . . . This congressional authority and the "semi-independent position" of Indian tribes have given rise to two independent but related barriers to the assertion of state regulatory authority over tribal reservations and members. *First, the exercise of such authority may be pre-empted by federal law.* (citing *Warren Trading Post Co. v. Arizona State Tax Comm'n.*) . . . *Second, it may unlawfully infringe "on the right of reservation Indians to make their own laws and be ruled by them."* (Citing *Williams v. Lee*) . . . The two barriers are independent because either, standing alone, can be a sufficient basis for holding state law inapplicable to activity undertaken on the reservation or by tribal members.

Id. at 142-43 (emphasis added and citations omitted).

The Supreme Court then noted that the most difficult questions arise whenever a state asserts authority over the conduct of non-Indians engaged in activities on Indian reservations. The court held:

In such cases we have examined the language of the relevant federal treaties and statutes in terms of both the broad policies that underlie them and the notions of sovereignty that have developed from historical traditions of tribal independence. *This inquiry is not dependent on mechanical or*

absolute conceptions of state or tribal sovereignty, but has called for a particularized inquiry into the nature of the state, federal, and tribal interests at stake, an inquiry designed to determine whether, in the specific context, the exercise of state authority would violate federal law.

Id. at 144-45 (citations omitted and emphasis added).

Turning to the specific facts of *Bracker*, the Supreme Court, just as it had done in *Warren*, noted the applicable federal statutes, and enumerated in detail the elements of extensive federal control over the harvesting and sale of Indian timber, underscoring the regulations which spell out:

. . . the federal purpose of development of Indian forests by Indian people for the purpose of promoting self-sustaining communities, to the end that the Indians may receive from their own property not only the stumpage value, but also the benefit of whatever profit it is capable of yielding and whatever labor the Indians are qualified to perform.

Id. at 147.

With respect to the roads in question, the Supreme Court pointed out that they are built and maintained by the Bureau and the Tribe and that Pinetop Logging spent substantial sums for maintaining and even building new logging roads. The Supreme Court then concluded:

In these circumstances we agree with petitioners that the federal regulatory scheme is so pervasive as to preclude the additional burdens sought to be imposed in this case. Respondents seek to apply their motor vehicle license and use fuel taxes on Pinetop for operations that are conducted solely on Bureau and tribal roads within the reservation. There is no room for these taxes in the comprehensive federal regulatory scheme. In a variety of ways, the assessment of state taxes would obstruct federal policies. And, equally important, respondents have been unable to identify any regulatory function or service performed by the State that would justify the assessment of taxes for activities on Bureau and tribal roads within the reservation.

Id. at 148-49.

Having thus examined federal policy and federal regulation of Indian timber, the Supreme Court questioned what interest the State of Arizona had in placing a tax on the non-Indian enterprise:

As noted above, this is not a case in which the State seeks to assess taxes in return for *governmental functions it performs for those on whom the taxes fall*. Nor have respondents been able to identify a *legitimate regulatory interest*served by the taxes they seek to impose. They refer to a general desire to raise revenue, but we are unable to discern a responsibility or service that *justifies* the assertion of taxes imposed for on-reservation operations conducted solely on tribal and Bureau of Indian Affairs roads. Pinetop's business in Arizona is conducted solely on the Fort Apache Reservation. Though at least the use fuel tax purports to `compensat[e] the state for the use of its highways,' no such compensatory purpose is present here. The roads at issue have been built, maintained, and policed exclusively by the Federal Government, the Tribe, and its contractors. We do not believe that respondent's [the state's] generalized interest in raising revenue is in this context sufficient to permit its proposed intrusion into the federal regulatory scheme with respect to the harvesting and sale of tribal timber.

Id. at 150 (emphasis added and citations omitted).

3. Analyzing The "Particularized Inquiry" Test. The Supreme Court has long recognized the rights of states to exercise their authority over non-Indians on Indian reservations in some circumstances. But as the *Warren, Williams* and *Bracker*cases demonstrate, in recent years the Supreme Court has also recognized that there comes a point at which the state's interest in an activity is so limited that it has no corresponding right to tax that activity. The Supreme Court's first hint of the "particularized inquiry" test came in *Washington v. Confederated Tribes of the Colville Reservation*, 447 U.S. 134 (1980), one of the cigarette tax cases discussed below. In *Colville*, the Supreme Court hinted that when a state seeks to tax non-Indians on Indian reservations, the interest that the state has in the subject of the tax must be *weighed* against *the interest of the Indian tribe*.

While the Tribes do have an interest in raising revenues for essential governmental programs, that interest is strongest when the revenues are derived from value generated on the reservation by activities involving the Tribes when the taxpayer is the recipient of tribal services. The State also has a legitimate governmental interest in raising revenues, and that interest is likewise strongest when the tax is directed at off-reservation value and when the taxpayer is the recipient of State services. As we have already noted, Washington's taxes are reasonably designed to prevent the Tribes from marketing their tax exemption to nonmembers who do not receive significant tribal services and would otherwise purchase their cigarettes outside the reservation. *Id*. at 156-57.

As we have seen, the competing interests of the state and the tribe in such cases led the Supreme Court to take the test first articulated in *Colville* and to characterize it for the first time in *Bracker* as the "particularized inquiry." Thus, the Supreme Court laid down the rule for the future that such cases require a "particularized inquiry" into the nature of not only state and tribal, but also federal interests at stake, a clear signal that all of those interests must all be weighed to see whether one preempts another. As we shall see, however, federal and tribal interests usually fall within the same balance pan and are weighed not against each other but against competing state interests.

4. *Central Machinery v. Arizona State Tax Comm'n.*, 448 U.S. 160 (1980). In this case, the Supreme Court again struck down the Arizona transaction privilege tax which it had held invalid as applied in *Warren Trading Post*. This time, the tax was applied to an on-reservation sale of farm machinery by an Arizona corporation to the Gila River Indian Tribe. The corporation *did not have a permanent place of business* on the reservation and *was not licensed by the federal government* to trade with Indians. Nonetheless, the Court still found that the tax was preempted by the extensive federal regulation of persons who trade with Indians. The state argued that the tax was valid because the *legal incidence* of the tax fell upon the non-Indian seller and not the Indian buyer of the goods. But clearly, the *economic incidence* fell on the Indian tribe since the price of the farm machinery was increased by the amount of the tax. This economic incidence was important, not because an economic burden on a tribe will *automatically* invalidate a state tax, but because the federal government had shown by its regulation of Indian traders that it was concerned with prices paid by Indians for goods on the reservation.

5. *Ramah Navajo School Board v. Bureau of Revenue*, 458 U.S. 832 (1982). In this case, the State of New Mexico attempted to tax gross receipts of a non-Indian corporation which contracted with the Ramah Navajo School Board to construct an Indian school on trust land in the Navajo Reservation. Obviously, New Mexico felt that setting the *legal incidence* of the tax on a non-Indian state corporation would avoid any unhappy entanglement with federal Indian law. The Supreme Court, however, examined the extensive federal statutes and regulations governing Indian education and the Ramah Navajo School Board, including the Snyder Act, 25 U.S.C. § 13, the Johnson-O'Malley Act, 25 U.S.C. § 452 *et seq*., and the Indian Self-Determination and Education Assistance Act, 25 U.S.C. § 450 *et seq*., and concluded that the federal regulatory scheme under which the tribal school board acted was so comprehensive as to preempt the state tax.

In answer to state arguments regarding state services rendered to the state-chartered non-Indian corporation, the Supreme Court suggested that off-reservation taxes should pay for off-reservation services to the contractor. While the Court recognized that the final economic incidence of the tax would be borne by the federal government, nevertheless the tax would necessarily result in depleting the amount of money available for construction of the Navajo school and thereby frustrate the federal policy of furthering Indian education and ultimately self-determination.

6. *Marty Indian School v. State of South Dakota* (1984 and 1987). The Marty School Board, Inc., a non-profit corporation under South Dakota law, sold soda pop, candy, and snacks to Indian children at the Marty Indian School on trust land inside an Indian reservation. The school was funded by the federal government through the Indian Self-Determination and Education Assistance Act and other federal programs, and was governed by extensive federal regulations and supervision of the BIA. The State of South Dakota attempted to tax sale of the snack items and argued that it had statutory authority under state law to tax a state non-profit corporation which could not claim to be an Indian tribe. Thus, the case is another example of a state's attempting to tax Indians by making the *legal incidence* of the tax fall upon non-Indians.

The trial court ignored state law and found that the federal preemption of Indian education, as spelled out by the Supreme Court in the *Ramah Navajo School Board* case, applied in this case as well and that while, at first blush, the sale of candy and snacks might seem unrelated to the goal of Indian education and self-determination, such sales created an atmosphere conducive to positive student attitudes and a good learning environment. Thus, the preemption analysis extends not only to vital elements of Indian education, such as provision of classrooms, but to incidental items which contribute to a positive learning environment. *Marty Indian School v. State of South Dakota*, 592 F. Supp. 1236 (D.S.D. 1984).

In 1987 the Eighth Circuit Court of Appeals applied the same reasoning to decide a suit between the same parties but involving a different tax: South Dakota's motor fuel tax. The Marty Indian School operated approximately 35 vehicles for transporting students, snow removal and other school business. Many of the vehicles belonged to and were licensed by the federal government and the school purchased fuel for its vehicles and stored it in tanks on trust land on the reservation. The court held that, despite use of the vehicles on state public highways inside the reservation and despite state expenditures on highway construction in the reservation, the

state's interest in obtaining revenue for its road programs was outweighed by federal preemption of Indian education and the federally-protected right of Indians to self-determination. *Marty Indian School v. State of South Dakota*, 824 F.2d 684 (8th Cir. 1987).

7. *New Mexico Taxation and Revenue Department v. Laguna Industries*, 855 P.2d 127 (1993). The Pueblo of Laguna obtained from Raytheon Service Company technical, training and management assistance on its reservation regarding the obtaining of federal defense contracts. New Mexico attempted to impose a gross receipts tax on income from such services on the ground that they did not constitute "trade" within the meaning of the federal trader statutes. Upon a challenge by the Pueblo to the imposition of such taxes, the New Mexico Supreme Court noted that the original Trade and Intercourse Act made express references to "boatmen" and "interpreters", thus making it clear that services were being federally regulated, as well as goods sold to Indians. The Court then noted that it must give the federal trader statutes "a sweep as broad as [their] language" and interpret them in the light of the intent of the Congress that enacted them, citing *Central Machinery*. Finding that nothing in the legislative history of the Trade and Intercourse Act supported the state's attempt to interpret "trade" narrowly, the Court held that trade includes services and struck down the tax as federally preempted.

D. TRIBAL TIMBER PRODUCTS.

As shown in *Bracker*, the federal government has a strong interest in tribal timber resource management. *Bracker* also makes it clear that a state tax imposed in connection with a tribal timber activity may be invalid, even though the legal incidence of the tax is upon a *non-Indian*. Some cases may not be as strong as *Bracker* because the non-Indian may not carry on its activities exclusively within the reservation. These cases, however, may have strengths of their own which must be carefully examined.

An excellent example of a case involving both on-reservation and off-reservation activities is *Hoopa Valley Tribe v. Nevins* (1984), 881 F.2d 657 (9th Cir. 1989), *cert. denied*, 494 U.S. 1055 (1990). In 1976 California passed a new, comprehensive timber yield tax designed to replace its former ad valorem tax on standing timber. The philosophy of the California legislature was that a "yield" tax which takes effect upon the date of harvesting timber is more fair than an annual tax on standing timber which forces property owners to harvest timber before the optimum harvest time in order to generate money to pay the annual tax. The yield tax is measured upon the value of the timber at the time of harvest. In order to deal with timber harvested from federal forest lands, the yield tax provided that the first non-exempt owner of the harvested timber, after the date of harvest, would be liable for the tax.

In 1976 the Hoopa Valley Tribe chartered the Hoopa Timber Corporation, a tribal enterprise, specifically to take advantage of tribal timber. The Hoopa Timber Corporation obtained a number of timber sale contracts from the BIA, manufactured logs from the harvested timber, and sold the logs to off-reservation purchasers. But on the advice of counsel, the Hoopa Timber Corporation was careful to see that all incidents of the log sales took place inside the reservation. Nevertheless, California notified all state timber purchasers that the purchases of Indian timber or logs were subject to the yield tax and began enforcement proceedings in a number of instances. The State's hope was that by placing the legal incidence of the tax on the

off-reservation based, non-Indian purchasers, it could get away with the tax even though it was defined as a tax upon the "yield" of the Indian forest at harvest, clearly an on-reservation activity.

The Tribe filed an action in the federal district court in San Francisco and in 1984 the federal judge ruled that the California tax was preempted by the extensive timber statutes and regulations just as in *Bracker* and entered a judgment against California in the sum of over $600,000. The case was sustained upon appeal to the Ninth Circuit Court of Appeals and the Supreme Court denied certiorari. It is important to note that in order to obtain the court's ruling that the state tax is illegal, the Tribe was careful to demonstrate with expert testimony that the standard timber industry practice in California is for the purchaser to deduct the amount of tax from its bid upon Indian timber or logs and, thus, to make the economic incidence of the tax fall upon the Indians.

E. TAXATION OF INDIAN MINERALS.

A unique problem exists in the area of state taxation of Indian minerals, such as oil, gas and coal.

1. Treaty-Established Reservations. A 1924 federal act authorized mineral leases of Indian land on treaty-established reservations for oil and gas production and authorized states to levy taxes on the production of those minerals. 25 U.S.C. § 398. The tax was to be paid from the royalties received by tribes from the leases.

2. Executive Order Reservations. A 1927 federal act essentially extended the 1924 Act to executive order reservations.

3. Comprehensive Legislation in 1938. However, in 1938, Congress enacted comprehensive legislation governing the leasing of tribal lands for mining purposes. 25 U.S.C. § 396a *et seq*. The Indian Mineral Leasing Act of 1938 repealed all laws which were inconsistent with it, although it did not explicitly mention the state's authority to tax under the 1924 Act or deal with the question of taxation in general.

4. *Montana, et al. v. Blackfeet Tribe*, 471 U.S. 759 (1985). With respect to *on-reservation, Indian-owned minerals*, the United States Supreme Court finally resolved the controversy over the effect of the 1938 Act on state tax authority under the 1924 and 1927 Acts in *Montana v. Blackfeet Tribe of Indians*. The Court held that the State of Montana could not tax the Blackfeet Tribe's royalty interests under oil and gas leases to non-Indians pursuant to the 1938 act. The taxes were paid to the state by the lessees and then deducted from royalty payments to the Tribe. The Court said that the 1924 Act does not authorize the imposition of the Montana oil and gas taxes to leases under the 1938 Act, and that the 1938 Act does not itself consent explicitly to state taxation nor implicitly by incorporating the 1924 Act's taxing authority.

The Court's opinion was grounded upon two rules of statutory construction applicable in Indian law:

a. States may tax Indians only when Congress has clearly consented; and
b. Statutes are to be construed liberally in favor of the Indians, with ambiguous provisions interpreted in their favor.

The Court said that when the 1924 Act is construed in accordance with the second rule, its taxing authorization, if it survives at all, applies only to leases issued under the 1924 Act.

5. *Crow Tribe v. Montana* (1987), 819 F.2d 895 (9th Cir. 1987), *summ. aff'd*, 484 U.S. 997 (1988). Montana sought to apply its severance and gross proceeds taxes to a non-Indian producer engaged in extracting coal from former tribal land outside the reservation under a lease from the Crow Tribe. The surface of the land had been sold by the government to non-Indians, but the government reserved to the Tribe the underlying mineral rights. The Ninth Circuit Court of Appeals found that the minerals constituted a part of the reservation, and that the 1938 Act applied. The court noted that the purposes of the 1938 Act were to: (1) revitalize tribal governments by giving them control over the leasing of their land; (2) promote tribal economic development; and (3) ensure that Indians receive the greatest return for their property. Montana argued that its taxes were not preempted by the 1938 Act, since the lessee, and not the Tribe, was the taxpayer.

The court rejected that argument, finding that the taxes hurt the Tribe's economic interests by reducing the amount of royalties and impairing the marketability of the coal. The court also rejected Montana's argument that the taxes were permissible under *Confederated Tribes* because they were the equivalent of a tax on sales to non-Indians; the court held that the *Confederated Tribes* rule did not apply where the value being taxed comes from the reservation. In addition to finding that the taxes were preempted by the 1938 Act, the court also held that the taxes were invalid because they did not show a "carefully tailored relationship between the severance tax revenues and the coal-related state services", and eroded the Tribe's sovereign authority over reservation affairs.

6. *Peabody Coal v. State of Arizona*, 761 P.2d 1094 (1988). In *Peabody Coal v. State of Arizona*, Peabody sought a refund of state tax paid on coal mined on the Navajo and Hopi Reservations and sold to non-Indian utilities. The Arizona Court of Appeals found that the tax did not burden the Tribes because the utilities reimbursed Peabody for the tax paid and the Tribes' royalties on the coal were based on Peabody's gross revenue; thus, when the utilities paid tax, the Tribes made more money. The court also found that Peabody's company headquarters was located off the reservations, and that Peabody and its employees benefitted greatly from state-funded services, such as schools and health and welfare programs, upon which Arizona expended far more than it received in tax revenues from Peabody. Accordingly, the court found no federal preemption of the Arizona tax despite extensive federal regulation of coal mining on the reservations.

7. *Granite Construction Company v. Arizona Department of Revenue*, 811 P.2d 345 (Az. App. 1990). In *Granite Const. v. Dept. of Revenue*, Granite Construction Company contracted with Peabody Coal to perform strip mine reclamation services. Arizona levied a transaction privilege tax upon Granite for such services, and Granite sought a refund of the tax in the Arizona court system, claiming the tax was preempted by the Navajo and Hopi Land Settlement

Act of 1974. On appeal, the Arizona Court of Appeals held that comprehensive federal regulation of mining activities on Indian reservations did not preempt the tax because: (1) the state expended substantial revenues, as discussed above, on the reservation to support the tax; and (2) the tax increased tribal royalties inasmuch as the Tribe's lease revenues were based on Peabody's gross coal revenues, which included full reimbursement of the transaction privilege tax.

8. *Cotton Petroleum Corporation v. New Mexico*, 490 U.S. 163 (1989). In *Cotton Petroleum Corporation v. New Mexico* a corporation was subjected to both a six percent tribal tax and an eight percent state tax on its oil and gas production on the Jicarilla Indian Reservation. The corporation argued that the tax was a violation of the Interstate Commerce Clause because the state tax was not apportioned in any way and that no credit was given for the tribal tax imposed. The corporation also argued that state taxes of $2,293,953 paid were excessive when compared with the small amount of state benefits it received, which amounted to only $89,384.

The Supreme Court rejected these arguments. It noted that the corporation paid both state and tribal taxes, still made a profit, and had plans to dig additional wells on the Reservation. The Court concluded that there was no economic impact on the Tribe. Therefore, the Court found that under the traditional theory of Indian preemption, it need not strike down the state tax.

The Supreme Court also rejected the Interstate Commerce Clause arguments. It found that a tribe cannot be equated to a state because the Commerce Clause draws a clear distinction between the two. Further, the Court held that so long as the state tax did not disrupt interstate commerce, it could not be required to be limited in amount to reimbursing New Mexico for the exact cost of specific services provided to the corporation. The Supreme Court held that under the traditional interstate commerce test, the state tax does not offend the Commerce Clause because it is applied to an activity with a substantial nexus with the taxing state, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the state to the corporation *and to the tribe*.

The *Cotton Petroleum* decision is a major blow to Indian tribes who wish to preempt state jurisdiction on the reservation. The decision represents a major departure from established Indian law principles for the following reasons:

a. The Court Distorted the Balancing Test. The Indian Mineral Leasing Act of 1938 and federal regulations govern all stages of oil and gas leasing and production on Indian reservations, including the bidding process, the setting of acreage limitations, royalty rates, methods of payment, regulation of lessees' operations, conservation of resources, prevention of waste, inspection, collection, auditing and security. In addition, the Jicarilla Tribe itself supplements federal statutes and regulations with its own which are administered by the tribal oil and gas administration. Nevertheless, the Supreme Court found the federal regulatory scheme not "exclusive" inasmuch as state law regulated well spacing and mechanical integrity of wells. The state offered no evidence as to any actual activity regarding well spacing and mechanical integrity inside the reservation, and the Tribe offered undisputed testimony that no state agent was ever on the reservation in that regard. Nevertheless, the state economist testified that since the state had provided spacing guidelines for the Tribe, some allocation of the state's expense

should be made to the reservation. The BIA adopted state spacing requirements for the reservation.

Based upon the foregoing, the Supreme Court found no federal preemption. This conclusion is clearly wrong. Earlier cases have found federal regulation of tribal timber and federal regulation of Indian education to create preemption. Federal regulation of tribal mineral leasing is easily shown to be as extensive as these activities. New Mexico had no legal authority regarding reservation well spacing and mechanical integrity of wells, nor did BIA adoption of state spacing requirements vest New Mexico with any such jurisdiction.

b. The Court Misconstrued Congressional Silence Regarding Taxation in the Indian Mineral Leasing Act of 1938. The Supreme Court interpreted congressional silence regarding application of state taxation in the 1938 Act as essentially incorporating the states' taxing authority contained in the 1924 Act. This interpretation of congressional silence is contrary to the Supreme Court's holding in *Montana v. Blackfeet Tribe of Indians*, 471 U.S. 759 (1985), and contrary to the rule that requires that statutes be construed liberally in favor of Indians.

c. The Court Ignored Federal Indian Policy Embodied in the Indian Reorganization Act of 1934. With the enactment of the IRA in 1934, federal Indian policy changed dramatically. Applying the rationale of *Bracker*, the Supreme Court should have held that imposition of the state tax "would threaten the overriding federal objective of guaranteeing Indians that they will receive . . . the benefit of whatever profit [their oil and gas reserves are] capable of yielding," and would "reduc[e] tribal revenues and diminis[h] the profitability of the enterprise for potential contractors." 448 U.S. at 149. Instead, the Supreme Court upheld the state tax. This constitutes a turning away from the federal Indian policy embodied in the IRA, is judicial legislation at its worst, and constitutes a substantial threat to the future of tribal sovereignty and tribal tax immunity.

d. The Court Utilized the Existence of General State Services to Tribal Members to Support Taxing Authority. After establishing the solid principle in virtually all previous preemption analysis cases that a state seeking to justify a tax must show that the tax proceeds are used to benefit or regulate *the activity taxed*, the Supreme Court, for the first time, considered general state services to Indians as justification for taxing authority. Previously, the Court has looked for a connection, or "nexus", between the state's regulatory involvement on a reservation and the tax the state wished to impose.

As we have seen, in *Ramah Navajo School District*, a state tax on school construction was struck down because state benefits to the Navajo Tribe were not in any way related to construction of schools on its Reservation. And in *New Mexico v. Mescalero Apache Tribe*, 462 U.S. 324 (1983), the Supreme Court struck down state hunting and fishing regulations and license fees on non-Indians on the Mescalero Reservation, despite state services to the Tribe, because no services were performed by New Mexico in connection with reservation hunting and fishing by non-members. Finally, in *McClanahan v. Arizona State Tax Comm'n*, 411 U.S. 164 (1973), the Supreme Court emphasized that conferring rights and privileges on Indians cannot affect their tax immunity. The Supreme Court well summarized this rule in *Mescalero*, 462 U.S. at 336:

[T]he exercise of state authority which imposes additional burdens on a tribal enterprise must ordinarily be justified by functions or services performed by the state in connection with the on-reservation activity.

The Ninth Circuit dealt even more explicitly with this issue in *Crow Tribe*. As we have already seen, in *Crow Tribe* the Ninth Circuit struck down a Montana state severance tax assessed against non-Indian operators of coal mines on the Crow Reservation. The Ninth Circuit invalidated the state tax both because it concluded that it was preempted by federal law and that it infringed on the Tribe's right to self-government. The Ninth Circuit held that the tax could not stand unless the state could show a "carefully tailored relationship between the severance tax revenues and the coal-related [state] services." *Id*., 819 F.2d at 901-02.

In *Cotton Petroleum*, the Court did not abolish the requirement of a connection between taxes and services; however, it found it significant that New Mexico provided "substantial services" to both the Jicarilla Tribe and Cotton, costing the state approximately $3,000,000 a year, although without finding any indication that these benefits were in any way related to the on-reservation activity the state sought to tax. It concluded that the value of benefits provided need not equal, nor even approximate, the amount of tax collected.

Following *Cotton Petroleum*, the Ninth Circuit in *Nevins* adhered to the nexus standard, having been persuaded that *Cotton Petroleum* did not change that rule. The court stated as follows:

Although California points to a variety of services that it provides to residents of the reservation and the surrounding area, none of those services is connected with the timber activities directly affected by the tax. To be valid, the California tax must bear some relationship to the activity being taxed. *See Crow Tribe*, 819 F.2d at 900. Showing that the tax serves legitimate state interests, such as raising revenues for services used by tribal residents and others, is not enough. *Id.* at 901. "To the extent that this [coal severance] tax is not related to the actual governmental costs associated with the mining of the Indian coal . . . the state's interest in acquiring revenues is weak in comparison with the Tribe's right to the bounty from its own land." *Crow Tribe v. Montana*, 650 F.2d at 1117 (citations omitted).

. . . .

The state's general interest in revenue collection is insufficient to outweigh the specific federal and tribal interests with which the timber yield tax interferes. The services provided by the state and county are provided to all residents . . . . California admits that there is no direct connection between revenues from the timber yield tax and the provision of services to tribal members or area residents generally.

. . . .

Because the timber yield tax does not fund services that directly relate to the harvesting of tribal timber and is otherwise unconnected with tribal timber activities, the timber yield tax should be preempted.

Hoopa Valley Tribe v. Nevins, 881 F.2d 657, 661 (9th Cir. 1989).

As the Ninth Circuit obviously understood, if there need be no nexus between the activity taxed by a state and state provision of services to reservation communities, then the basis upon which to stop almost any state tax on almost any non-Indian activity is severely weakened. Most

states do provide some services--social services, education--on many reservations simply because members of Indian tribes are also citizens of the United States.

e. The Beginning of Numerical Analysis. In *Cotton Petroleum*, the Supreme Court seems to begin a questionable practice of allowing the question of state on-reservation tax authority to turn at least partly on numerical analysis. In the absence of evidence that either the legal or economic incidence of the state's eight percent severance tax fell on the Tribe, coupled with evidence that the corporation had plans to drill additional wells on the reservation, the Supreme Court concluded that the state tax did not "impose a substantial burden on the Tribe" and decided that the tribal interest was "indirect and . . . insubstantial." Thus, the Supreme Court decided that the state tax did not interfere with tribal self-government. But the tax struck down by the Supreme Court in *Warren Trading Post*, 380 U.S. 685 (1965), was only two percent, and the combined tax struck down by the Supreme Court in *Bracker* was less than one percent and, indeed characterized by the dissenters in *Bracker* as "relatively trivial" and "unlikely to have a serious adverse impact on the tribal business." 448 U.S. at 159.

In *Cotton Petroleum* the Supreme Court bolstered its conclusion that the state tax did not burden the Tribe by pointing to the Corporation's plan to drill additional wells. But the wells planned by the Corporation are "infill" wells; that is, wells drilled between existing producing wells to increase the efficiency of drainage on leased lands. Infill wells are essentially "no risk" propositions because of almost certain production. It cannot be seriously argued that the state severance tax, when added to the tribal severance tax to produce 75% higher on-reservation than off-reservation taxes within the state, will not deter future drilling and seriously affect the Tribe's central source of income.

f. A Warning Note. The principles of Indian preemption jurisprudence developed by the Supreme Court in the preceding cases have been undermined in *Cotton Petroleum*, 490 U.S. 163 (1989). That 6-to-3 decision of the Supreme Court dangerously misapplies the traditional tools of Indian preemption analysis by adopting what the dissenting opinion of Justice Blackmun termed the principle of "inexorable zero;" that is, a requirement that the state be *entirely* excluded from a sphere of activity and provide *no* services to Indians or non-Indians engaged in commerce on a reservation before federal preemption can be found to exist.

In addition, the *Cotton Petroleum* decision totally ignores the requirement that statutes enacted to protect Indians be interpreted in their favor and, in fact, seemed to adopt a contrary principle that silence regarding state taxation in the Indian Mineral Leasing Act of 1938 should be interpreted as *incorporating* state taxing authority contained in a previous act. Finally, in the *Cotton Petroleum* decision, the Supreme Court totally ignored the philosophy of harmonizing tribal leasing with the goals of the Indian Reorganization Act "to ensure that Indians receive the greatest return from their property." *Montana v. Blackfeet Tribe of Indians*, 471 U.S. 759, 767 n.5 (1985).

9. The Future After *Cotton Petroleum*. All in all, the above considerations make it clear that the six-person majority led by Justice Stephens may well seek to dismantle established principles of tribal sovereignty and tribal tax immunity. Justices Brennan, Marshall, White, and Blackmun have retired and have been replaced by Justices David Souter, Clarence Thomas, Ruth Bader

Ginsberg and Stephen Breyer. Thus, the question of how these appointees to the Supreme Court will vote on Indian law issues becomes critical.

F. THE FUTURE OF THE INFRINGEMENT AND FEDERAL PREEMPTION TESTS.

1. The "Geographical Component and the Per Se Rule".

a. The Geographical Component. In *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980), the Supreme Court rejected the argument that Congress must forbid a state to impose taxes on non-Indians engaged in commerce on Indian reservations before it is barred from doing so. It said that a tribe's power over its own reservation was still an important consideration in deciding whether a state tax on non-Indians was permissible. The Court held:

The Court has repeatedly emphasized that there is a *significant geographical component to tribal sovereignty, a component which remains highly relevant to the preemption inquiry*; though the reservation boundary is not absolute, it remains an important factor to weigh in determining whether state authority has exceeded the permissible limits. "The cases in this Court have consistently guarded the authority of the Indian governments over their reservations."

Id. at 151 (citations omitted).

The "geographical component" has a negative side also. *Mescalero Apache Tribe v. Jones*, 411 U.S. 145 (1973), involved an attempt by New Mexico to impose a use tax upon material used by the Tribe to construct a ski resort on Forest Service land outside the reservation and to impose a school tax on its gross receipts. A number of unique features of the fact pattern of the case call for scrutiny. Operating in its corporate capacity under section 17 of the Indian Reorganization Act, 25 U.S.C. § 477, the Tribe leased, for a term of 30 years, land inside the Lincoln National Forest upon which it constructed its ski resort, the Inn of the Mountain Gods, including several ski lifts and associated buildings. New Mexico levied a gross receipts tax upon receipts of the ski resort and upon sales of services and tangible property and use taxes upon materials used to construct the ski lifts and buildings.

The Supreme Court noted that the Tribe acted under its corporate charter, rather than under its constitution, but held that the question of tribal tax immunity could not be made to turn on the particular form in which the Tribe chose to conduct its business. Thus, the Supreme Court held, essentially, that a tribal corporate entity chartered under the IRA is equivalent to the tribe itself with respect to federal tax immunities. The Supreme Court held that in the special area of state taxation, absent a granting of jurisdiction by the federal government to the state, or federal statutes permitting it, a state may not tax Indian reservation lands or Indian income from activities carried on within the boundaries of the reservation.

The Supreme Court held that, although the leased Forest Service land was outside the reservation, it was basically equivalent to tribal trust lands because it would have been meaningless for the United States, which had title to the forest, to convey title to itself for the use of the Tribe. Because the Supreme Court found that the ski lifts and buildings were permanently attached to the real property, the state tax upon use of the ski lifts became the equivalent of a tax upon use of the land; therefore, the Supreme Court struck down the use tax.

But the Supreme Court held that when the Mescalero Apache Tribe went *off* its Reservation to operate a business, its receipts from the business were subject to the state gross receipts tax. For that purpose, the status of the Forest Service land seemed to make no difference. Given the fact that an Indian tribe has sovereign immunity from suit in any court, state or federal, it is difficult to see how New Mexico could enforce its gross receipts tax against the Mescalero Apache Tribe. Curiously, the Supreme Court did not mention this aspect of the case although in *McClanahan v. Arizona St. Tax Comm'n*, 411 U.S. 164 (1973), decided the same day, the Supreme Court, in striking down a state income tax on individual tribal members, noted that nowhere did Arizona explain how its tax could be imposed or collected, and stated that unless Arizona was willing to defend the position that it could constitutionally administer a tax system without judicial intervention, the absence of jurisdiction would seem to dispose of the case. It would also seem to dispose of New Mexico's gross receipts tax in *Mescalero*! Apparently, the geographical component will continue to support and to insure the future effectiveness of both the interference and federal preemption tests, particularly in light of the case discussed below.

b. The Per Se Rule. The strength of the "geographical component" was set in stone by the Supreme Court in *California v. Cabazon Band of Indians*, 480 U.S. 202 (1987). Although the case was not a tax case but involved California's attempt to prohibit high stakes bingo on the Cabazon Indian Reservation in California, nonetheless, the Supreme Court took the opportunity to establish the "per se" rule with respect to state attempts to tax Indians and Indian property on their reservations. The Court stated:

In the special area of state taxation of Indian tribes and tribal members, we have adopted a per se rule. In *Montana v. Blackfeet Tribe*, 471 U.S. 759 (1985), we held that Montana could not tax the Tribe's royalty interests in oil and gas leases issued to non-Indian lessees under the Indian Mineral Leasing Act of 1938. We stated: "In keeping with its plenary authority over Indian affairs, Congress can authorize the imposition of state taxes on Indian tribes and individual Indians. It has not done so often, and the Court consistently has held that it will find the Indians' exemption from state taxes lifted only when Congress has made its intention to do so unmistakably clear." *Id.*, at 765. *We have repeatedly addressed the issue of state taxation of tribes and tribal members and the state, federal, and tribal interests which it implicates. We have recognized that the federal tradition of Indian immunity from state taxation is very strong and that the state interest in taxation is correspondingly weak. Accordingly, it is unnecessary to rebalance these interests in every case*. In *Mescalero Apache Tribe v. Jones*, 411 U.S. 145, 148 (1973), we distinguished state taxation from other assertions of state jurisdiction. We acknowledged that we had made repeated statements "to the effect that, even on reservations, state laws may be applied unless such application would interfere with reservation self-government or would impair a right granted or reserved by federal law. . . . *Even so, in the special area of state taxation, absent cession of jurisdiction or other federal statutes permitting it, there has been no satisfactory authority for taxing Indian reservation lands or Indian income from activities carried on within the boundaries of the reservation, and McClanahan v. Arizona State Tax Comm'n, [411 U.S. 164 (1973)], lays to rest any doubt in this respect by holding that such taxation is not permissible absent congressional consent*." *Ibid*. (emphasis added).

California v. Cabazon Band of Indians, 480 U.S. 202, ___ n.17 (1987) (some emphasis added).

2. The Dominance of Federal Preemption. The federal preemption doctrine has been the major tool used by courts to invalidate state taxes imposed on Indian reservations. Federal preemption has so often been the basis for invalidating state taxes imposed on reservation Indians that it can now be said that whenever the *legal incidence* of the state tax falls on a reservation Indian engaging in activity on the reservation or on an Indian tribe operating within the reservation, the state tax must fail.

a. *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980). The federal preemption doctrine now has greater importance in cases of state taxation of *non-Indians* on the reservations. As we have already seen in *Bracker*, the Supreme Court struck down the State of Arizona motor carrier license tax and use fuel tax imposed on a non-Indian enterprise doing business within the Fort Apache Reservation. The non-Indian company felled and transported timber within the reservation under contract with the Tribe. The company's activities were performed *exclusively within* the reservation. The state taxes were held *preempted* by federal law. The court said that the federal government had completely taken over the regulation of harvesting, sale and management of tribal timber, leaving no room for additional burdens imposed by the state.

One of the federal interests involved was in assuring that the tribe would benefit from the profits from timber sales. *Bracker* is important because it shows that even where the *legal incidence* of a state tax falls on *non-Indians* on a reservation, the state tax may still be invalid. The *economic incidence* of the tax fell on the White Mountain Apache Tribe because it increased the cost of doing business with the non-Indian company. However, the *economic incidence* alone was not enough to invalidate the tax. The court said:

Of course, the fact that the economic burden of the tax falls on the Tribe does not by itself mean that the tax is preempted, as *Moe v. Salish & Kootenai*, makes clear. Our decision today is based on the preemptive effect of the comprehensive federal regulatory scheme, which, like that in *Warren Trading Post Co. v. Arizona State Tax Comm'n*, leaves no room for the additional burdens sought to be imposed by state law.

Bracker, 448 U.S. at 151 n.15 (citations omitted).

Despite the fact that the Supreme Court specifically grounded its decision upon federal preemption, it referred indirectly to the interference test by pointing out that the Arizona tax would interfere with the Tribe's ability to comply with federal law and policies governing Indian timber by leaving both the Tribe and its contractors with reduced sums with which to pay out federally-required expenses, such as those required for reforestation, fire control, wildlife promotion, road improvement, safety inspections and the general policing of the forest. Thus, it would seem, upon analysis, that the Arizona taxes should fall under the interference test alone.

b. *Herzog Brothers Trucking Inc. v. New York Tax Comm'n.*, 533 N.E.2d 255 (1987). Following the Supreme Court's lead in *Warren Trading Post*, the New York Court of Appeals struck down New York's taxing scheme with respect to sales of motor fuel on Indian reservations. State law imposed the tax at the time the fuel was first imported into the state; thus, the distributor, who was also a federally-licensed Indian trader, paid the taxes and then included them in its wholesale price. Whenever the ultimate consumer was an Indian, a refund or credit was allowed. The court rejected the argument that this collection scheme was simply a "minimal

burden" authorized by the Supreme Court in *Moe v. Confederated Salish and Kootenai Tribes*, 425 U.S. 463 (1976), and *Confederated Tribes*. Instead, the Appeals Court held that the Federal Indian Trader Licensing Laws preempted the field, and no state regulation of the federally-licensed Indian trader was permitted.

c. *Oklahoma Tax Commission v. Chickasaw Nation*, ____ U.S. ____, 115 S.Ct. 2214 (1995). Oklahoma's fuels tax is levied on retailers, not on distributors or consumers. The Supreme Court held the tax as applied to tribal retailers illegal, and found no need to balance federal, state and tribal interests. The Court stated:

[W]hen a State attempts to levy a tax directly on an Indian tribe or its members inside Indian country, rather than on non-Indians, we have employed, instead of a balancing inquiry, "a more categorical approach--`[A]bsent cession of jurisdiction or other federal statutes permitting it,' we have held, a State is without power to tax reservation lands and reservation Indians."

115 S. Ct. at 2220 (citations omitted). As discussed below, however, the Court went on to uphold a state income tax imposed on tribal members who resided outside Indian country, although the income was earned from their employment by the Tribe within Indian country. That ruling drew the dissent of Justice Breyer, joined by Justices Stevens, O'Connor and Souter.

3. Summary. The federal preemption doctrine has played a major role in protecting Indian tribes and individual Indians from state taxes whenever the taxes are imposed directly upon them. It has played an even greater role in warding off state taxes where the tax itself is imposed on non-Indians, but the *economic impact or incidence* of the tax is felt by the tribe. The economic impact on an Indian tribe of a state tax on a non-Indian alone, however, is not enough to invalidate the state tax. In the federal preemption cases, the tribes had to show economic impact coupled with extensive federal concern with the activity which suffers from the economic impact of the tax.

Federal preemption has been based upon Indian treaties and general federal legislation, such as the Indian Reorganization Act of 1934, and disclaimers of jurisdiction over Indian lands found in state constitutions. These have generally been enough to support individual Indian and tribal exemptions from state taxes imposed *on Indians and tribes on their reservations*. Whenever the tax is imposed on *non-Indians* within the reservation or on tribes *outside* their reservations, the courts look for a much more specific intention on the part of the federal government to preempt the subject of the tax the state seeks to impose. Whenever the legal incidence of the tax is on non-Indians, it will be important for tribes to show that the federal government extensively regulates the area, as in *Bracker* or *Ramah*, or that the tribe itself has *a significant interest* in the transaction in which the tax is imposed which outweighs any interests of the state. If the tribe is marketing only a tax exemption, specific federal intent to preempt is required. If, however, the tribe is marketing some value that is generated on-reservation, the general federal statutes, which encourage tribal self-government and economic development and prohibit state jurisdiction over reservation Indians, may be sufficient to defeat a state tax with the federal preemption doctrine.

The states have been actively asserting a right to tax non-Indian activity which takes place on reservations. As we have seen in the *Ramah Navajo School Board* case, New Mexico attempted to tax gross receipts received by the non-Indian, state-chartered contractor even out of

funds specifically appropriated by Congress for construction of school facilities on the Navajo Reservation. In *Mescalero Apache Tribe v. O'Cheskey*, 625 F.2d 967 (10th Cir.), *cert. denied*, 460 U.S. 959 (1981), the Tenth Circuit Court of Appeals upheld a New Mexico gross receipts tax imposed upon several non-Indian contractors who did construction work for the Mescalero Tribe on a resort complex and other projects on reservation lands. The court found that the tax was not preempted by federal law because reservation construction work is not heavily regulated by the federal government. The court found no infringement of tribal self-government because the *incidence* of the tax was on the non-Indians rather than the Tribe. A similar holding occurred in *Tiffany Construction Co., Inc. v. Bureau of Revenue*, 629 P.2d 1225 (1981), a New Mexico Supreme Court decision.

G. THE CIGARETTE TAX CASES.

1. *Moe v. Confederated Salish and Kootenai Tribes*, 425 U.S. 463 (1976). *Moe* continued the principles laid down in *McClanahan* and struck down Montana taxes imposed upon Indian personal property located within an Indian reservation; a Montana vendor license fee imposed on Indian smokeshop operators; and the Montana cigarette sales tax as applied to on-reservation sales of cigarettes by Indians to Indians, because they were in conflict with federal law as set forth in the *McClanahan* case. The *legal incidence* of these taxes and fees was clearly upon Indians on the reservation.

But it held that the cigarette sales tax, as applied to on-reservation sales of cigarettes by Indians to *non-Indians*, was valid. According to the Supreme Court the legal incidence of the tax was clearly on non-Indians, although the economic incidence fell on tribal Indians because non-Indians would no longer buy cigarettes from reservation smokeshops if they carried the state sales tax. The Court obviously felt that the State of Montana possessed power over non-Indians doing business within the reservation.

To the Tribes' assertion that requiring Indian retailers to become involuntary agents for Montana constitutes a gross interference with the Tribes' freedom from state regulation, the Supreme Court held that the state requirement that the Indian retailer collect a tax from non-Indians is a minimal burden which neither frustrates tribal self-government nor runs afoul of congressional statutes dealing with Indian affairs.

2. *Washington v. Confederated Tribes of the Colville Reservation*, 447 U.S. 134 (1980). Prior to the time *Moe* reached the Supreme Court, the Colville Tribes, aware of the dangers posed by the sparse facts of *Moe*, carefully constructed a tribal tobacco enterprise utilizing the protection of every available element of federal and Indian law. The Tribes enacted a tobacco ordinance which established the Tribes as the wholesalers of all cigarettes imported into and sold on the reservation. The ordinance required the out-of-state purchase of all cigarettes, thus utilizing applicable principles of interstate commerce. Next the ordinance required federal traders' licenses of all out-of-state wholesale sellers and of retail sellers of cigarettes on the reservation, thus utilizing the federal trader statutes and the *Warren Trading Post* principles.

The ordinance required that all retail sellers be enrolled tribal members and provided that their businesses were tribal businesses, which they were licensed to operate on behalf of the

Tribes pursuant to tribal licenses issued under the ordinance. The ordinance adopted the federal trader regulations and added its own, including restrictions on sales to minors, a two-carton sale limit, a requirement that all retail sales outlets be on Indian trust land and a retail sales tax upon all cigarette sales to non-Indians. The ordinance provided that tax revenues be devoted, in part, to social services to tribal members, such as a home for elderly tribal members, alcohol rehabilitation and the like.

Based upon the strength of this foundation, the Tribes were able to obtain an injunction against state imposition of cigarette taxes for almost eight years, between 1973 and 1980. But when the matter reached the Supreme Court after it had ruled on *Moe*, the Supreme Court again upheld a cigarette sales tax as applied to on-reservation sales of cigarettes by Indians to non-Indians. The Court held that the legal incidence of the tax was upon the purchaser, and therefore, valid as applied to sales to non-Indians. The Tribe argued that even though the legal incidence was upon the non-Indian purchasers, other factors not present in *Moe* invalidated the tax. The difference in this case was that the tribes had imposed their own tax on cigarette sales and further, had taken part in the marketing of the cigarettes themselves. These measures obviously gave the tribes a *greater interest* in cigarette sales than the tribe in the *Moe* case had. The belief was that this tribal interest would be enough to displace the state's right to impose its tax. The theories used were: (a) The state tax was preempted by federal statutes and policy which promoted tribal self-government and economic development; (b) The state tax infringed on the right of the tribes to govern themselves. Put another way, the state tax was *preempted* by tribal laws regulating and taxing cigarette sales; and (c) The state tax violated the Indian Commerce Clause because it imposed an undue burden upon Indian commerce.

The Court rejected all three theories.

3. *Oklahoma Tax Comm'n v. Potawatomi Indian Tribe*, ___ U.S. ___, 111 S.Ct. 905 (1991). The Supreme Court reaffirmed the principle of *Moe* and *Confederated Tribes* in *Oklahoma Tax Comm'n v. Potawatomi Indian Tribe*. The cigarette sales in question were conducted by the Tribe itself on tribally-owned trust land not officially designated as an Indian reservation. Oklahoma urged the Supreme Court to apply the rule of *Mescalero,* in which the Supreme Court held:

Absent express federal law to the contrary, Indians going beyond reservation boundaries have generally been held subject to nondiscriminatory state law otherwise applicable to all citizens of the State.

411 U.S. at 148-49. The Supreme Court declined the invitation and, in fact, strengthened the geographical component by holding that determination of whether land is "Indian country" is whether it has been validly set apart for the use of Indians under the superintendence of the federal government, not whether the land is officially designated a reservation. Thus, concluded the Court, trust land "validly set apart" qualifies as a reservation for tribal immunity purposes. The Supreme Court upheld tribal sovereign immunity against a state claim for $2.7 million uncollected and unpaid taxes, and answered the state's complaint that sovereign immunity denied the state justice by suggesting five possible state remedies:

1. The Supreme Court had never held that individual agents or officers of a tribe could not be held personally liable for damages for failure to collect and remit valid state taxes;

2. The state could seize untaxed cigarettes in shipment to the reservation;
3. The state could collect cigarette taxes from the wholesalers off the reservation;
4. The state could enter into a tax collection compact with the Tribe; and
5. The state could seek congressional legislation.

4. *Oklahoma Tax Commission v. City Vending of Muskogee, Inc.*, 835 P.2d 97 (1992). Seizing the second remedy suggested by the Supreme Court, the State of Oklahoma required cigarette wholesalers to affix state cigarette stamps to all cigarettes sold within the State. In *Oklahoma Tax Commission v. City Vending of Muskogee, Inc.* (1992), the Oklahoma Supreme Court upheld the tax, even though recognizing that the Tax Commission might have acted in excess of its authority. The Court pointed out that City Vending, as claimant of a tax exemption, bore the burden of proof of sales to tribal members, which would justify the claimed exemption, but failed to provide a proper record showing that any of the cigarettes wholesaled by City Vending to the Creek Nation were actually sold to tribal members. Thus, Oklahoma has taken the first step in plugging what it considers to be an illegal loophole in its cigarette tax collection scheme, and can be expected to take further steps with respect to out-of-state wholesalers.

5. Imposing "Minimal Burdens" on Indian Cigarette Sellers. In *Moe*, the Supreme Court said that a state could require Indian sellers to collect state tax from non-Indian purchasers as a "minimal burden" designed to insure that non-Indian purchasers pay the lawful tax. 425 U.S. at 483. Just how much of a burden a state can impose remains an open question.

In *Confederated Tribes* the Court upheld a state requirement that tribes affix state tax stamps before selling to non-Indians. The Court also approved imposing recordkeeping requirements as to both non-Indian and Indian sales to the extent "reasonably necessary as a means of preventing fraudulent transactions." 447 U.S. at 160. Finally, the Court upheld the state's authority to seize shipments of untaxed cigarettes off the reservation where a tribe refuses to comply with valid state tax laws. The Court declined to decide whether states could carry out seizures within Indian reservations, noting that such action is "considerably different" from off-reservation seizures. *Id.*

As a further means of enforcing their cigarette taxes, some states require that delivery of unstamped cigarettes to Indian vendors be made only in quantities approved by the state in advance. This arrangement clearly puts a state in the position effectively to deny a tribe its right to be free from state taxation. Nevertheless, the Washington Court of Appeals upheld the advance-approval requirement in *Gord v. State Department of Revenue*, 749 P.2d 678 (1987), 50 Wn. App. 646 (1987).

Keeping track of an Indian cigarette retailer by requiring him to obtain a state license and permit, goes beyond the "minimal burden" authorized by the Supreme Court in *Moe*. In *State, ex rel. Tax Comm'n v. Bruner*, 815 P.2d 667 (Okl. 1991), the Oklahoma Supreme Court held that the Indian Commerce Clause in the United States Constitution limits state authority over Indian cigarette retailers operating in Indian country and prohibits the state from imposing its license and permit requirements.

Meanwhile, the State of New York, facing similar difficulty, adopted regulations which required state cigarette wholesalers to prepay taxes on cigarettes delivered to state Indian reservations in excess of a predetermined figure calculated upon the "probable demand of qualified Indian consumers in the trade territory." The regulations required that each such wholesaler must: (1) request a copy of the prospective retailer's tax exemption certificate; (2) keep records of his sales; (3) obtain approval prior to each sale, either from the tribe or the Department of Taxation and Finance, of the quantity purchased; and (4) after completion of the sale, forward to the Department a copy of the prospective retailer's tax exemption certificate. In *Milhelm Attea & Bros., Inc. v Department of Taxation and Finance of the State of New York*, 615 N.E. 2d 994 (1993), the New York Court of Appeals struck down the regulations on the ground that they impose not "minimal" but "significant" burdens on wholesalers and are thus preempted by the federal trader statutes, specifically because they interfere with the statutory authority of the Commissioner of Indian Affairs to determine the kind and quantity of goods and the prices at which such goods shall be sold to the Indians.

But on appeal to the U.S. Supreme Court, however, the case was reversed. *Department of Taxation and Finance of New York v. Milhelm Attea & Bros., Inc.*, ____ U.S. ____, 114 S. Ct. 2028 (1994). The Supreme Court carefully considered and rejected the reasoning of the New York court by pointing out that while the broad language of *Warren* suggested that Indian traders are immune from state regulation reasonably necessary to the assessment or collection of lawful state taxes, the Supreme Court had undermined that proposition in the subsequent cigarette tax cases, *Moe, Colville, and Oklahoma Tax Comm'n v. Potawatomi Indian Tribe*. The Supreme Court then held:

In particular, these cases have decided that States may impose on reservation retailers minimal burdens reasonably tailored to the collection of valid taxes from non-Indians . . . It would be anomalous to hold that a State could impose tax collection and book-keeping burdens on reservation retailers who are enrolled tribal members, including stores operated by the tribes themselves, but that similar burdens could not be imposed on wholesalers, who often (as in this case) are not.

114 S. Ct. at 2036.

New York received another boost from the Supreme Court when, following the *Moe* opinion, the state required Indian retailers on state Indian reservations to collect and remit state cigarette taxes on sales to non-Indians. In *Snyder v. Wetzler, Commissioner of Taxation and Finance*, 193 A.D. 2d 329 (1993), the New York Appellate Division noted that the legal incidence of the tax was upon the consumer, not the Indian retailer, then pointed out that the Supreme Court stated in*Oklahoma Tax Comm'n v. Potawatomi Indian Tribe*, 111 S.Ct. at 912:

We have never held that individual agents or officers of a tribe are not liable for damages in actions brought by the State. See *Ex parte Young*, 209 U.S. 123, 28 S.Ct. 441, 52 L.Ed. 714 (1908).

Based upon the principles of these cases, the New York Appellate Division upheld the tax.

Another open question concerns a state's authority to enforce its cigarette tax laws by arresting Indian vendors on their reservation and charging them with crimes in state courts. The

tribe itself should have sovereign immunity from any such enforcement actions, under the Ninth Circuit Court's 1985 opinion in *California State Board of Equalization v. Chemehuevi Indian Tribe*, 474 U.S. 9 (1985). As for individual Indian vendors, the basis for state criminal jurisdiction is questionable. Even where a state has been granted general criminal jurisdiction over Indians on reservations under federal laws, such as Pub. L. 83-280, the Supreme Court's decision in *California v. Cabazon Band of Indians*, 480 U.S. 202 (1987), makes it clear that states generally do not possess the power to use criminal penalties to enforce regulatory laws against Indians on reservations. Arguably, the sole enforcement mechanism available to a state is the seizure of cigarettes outside the reservation. Nevertheless, in *State v. Brooks*, 763 P.2d 707 (1988) the Oklahoma Criminal Appeals Court ruled that *implicit* in the Supreme Court's decision that a state may impose its tax collecting and recordkeeping requirements on a tribe is the authority to apply its criminal laws where those requirements are not observed.

Trafficking in contraband cigarettes also runs the risk of federal prosecution. In *United States v. Baker*, 63 F.3d 1478 (9th Cir. 1995), transporting unstamped cigarettes into Washington without preapproval by the Department of Revenue was held to violate the Contraband Cigarette Trafficking Act, 18 U.S.C. §§ 2341-42, and also constituted an element in violation of the Racketeer Influenced and Corrupt Organizations Act. *See also United State v. Gord*, ___ F.3d ___ (9th Cir., Mar. 1, 1996).

As we have already seen in *Snyder v. Wetzler, Commissioner of Taxation and Finance* (1993), in the civil arena the picture is rapidly changing due to the Supreme Court's pronouncements in *Oklahoma Tax Comm'n v. Potawatomi Indian Tribe.*The Supreme Court did not discuss criminal penalties in that case, but by inviting suit against individual agents or officers of the tribe, the Supreme Court implied that tribal sovereign immunity does not protect them from the state.

States, ever vigilant to legal possibilities of increasing their tax revenues at the expense of Indians, continue to seek out every possible legal advantage. In *Buzzard and United Keetoowah Band of Cherokee Indians v. Oklahoma Tax Commission*, 992 F.2d 1073 (1993), the Tenth Circuit Court of Appeals upheld the Oklahoma cigarette tax on cigarette sales made by the Keetoowah Cherokee Tribe on restricted land purchased in fee simple by the Tribe with its own funds. The Tenth Circuit affirmed the holding of the district court that such restricted land was not "validly set apart for the use of the Indians as such, under the superintendency of the Government" (quoting from *Oklahoma Tax Comm'n v. Potawatomi Indian Tribe*,111 S.Ct. at 910 (1991), and therefore was not "Indian country." The Court held that superintendency over the land requires an active involvement of the federal government, which did not exist in this case. The decision makes it clear that the courts will look for holes in the "geographical component" to allow the incursion of state taxes on Indian reservations. Perhaps the culmination of such an effort is *Lummi Indian Tribe v. Whatcom County, Washington*, 5 F.3d 1355 (1992), *cert. denied*, 62 USLW 3757 (1994).

H. MARKETING RESERVATION-GENERATED VALUE.

1. The General Rule. Perhaps the most important emerging legal doctrine in the area of protecting tribal tax immunity is the doctrine of reservation-generated value. The doctrine first

appeared in the Supreme Court's opinion in *Confederated Tribes*. Unfortunately, by the time the *Confederated Tribes* case reached the Supreme Court, it had already decided the *Moe* case, in which the Salish and Kootenai Tribes had *conceded* legality of the state cigarette tax against non-Indians, but challenged the authority of the state to require Indian retailers to collect the tax. Given this concession, it is perhaps not surprising that the Supreme Court stretched the law, characterizing the collection requirement as a "minimal burden designed to avoid the likelihood that in its absence non-Indians purchasing from the tribal seller will avoid payment of a concededly lawful tax." At the heart of *Moe* was the Supreme Court's feeling that it was simply not willing to allow the non-Indian purchaser to flout his legal obligation to pay the concededly legal tax and for reservation Indians to benefit from sheer tax avoidance.

The Supreme Court's repugnance to tax avoidance by non-Indian cigarette purchasers led it to refine its rule and conclude that the Tribes did not have a significant enough involvement with the value or product on which the state wished to impose its sales tax. The Colville Tribes and tribal members took no part in the growing of tobacco, its curing or processing, or in the manufacture of or packaging of cigarettes. Instead, the cigarettes sold under the Tribes' cigarette enterprise were manufactured in a cigarette manufacturing plant in North Carolina by North Carolina labor using tobacco grown in North Carolina. After the cigarettes were manufactured and packaged, they were shipped to the Colville Reservation and sold at retail. The Supreme Court expressed the belief that the *only* reason the Tribes had commerce in cigarettes with non-Indians in the first place was the potential freedom from the state sales tax. It said that all the Tribes were marketing, in other words, was a *tax exemption* and not a *reservation-generated value*.

The lack of a sufficient Indian interest in the product subjected to the tax was fatal to the position of the Confederated Tribes, even though they had carefully crafted their tobacco ordinance and their tribal tobacco enterprise to take advantage of all aspects of tribal sovereignty, tribal tax immunities and interstate commerce law. In the aftermath of the *Moe* case in which the Salish and Kootenai Tribes had failed to take advantage of those legal protections, the legal structure of the tribal cigarette enterprise, standing alone, could not defeat the state sales tax.

The growing importance of the doctrine of reservation-generated value was illustrated when, in *California State Board of Equalization v. Chemehuevi Indian Tribe*, 474 U.S. 9 (1985) (*per curiam*), the Supreme Court shocked Indian country by summarily reversing a ruling in favor of the Tribe without even affording the parties prior notice or an opportunity to file briefs on the merits. The lower court, the Ninth Circuit Court of Appeals, had held that the legal incidence of the California cigarette tax fell upon the Indian seller and was, therefore, invalid as applied. That court reasoned that, unlike the Washington State statute in *Confederated Tribes*, the California statute contained no explicit provision requiring the tax to be passed on to the purchaser when the seller could not be taxed. But the Supreme Court held that no explicit statement that the tax be passed through to the purchaser was required in order for it to find that a state tax, which by its terms falls on the seller, is automatically passed on to the purchaser when the seller is untaxable. The Supreme Court arrived at this conclusion by way of a test which it said would be derived from its earlier decisions in *Moe* and *Confederated Tribes*, namely, "nothing more than a fair interpretation of the taxing statute as written and applied." 474 U.S. at 11.

The Court said it would require a much more specific indication that the federal government wished to bar the sales tax before it would hold that state sales tax immunity was federally-preempted as part of the plan for tribal economic development and self-government encouraged by federal statutes. *Id*. Again, the Court said that there would be no infringement on tribal government unless the Tribes had a sufficient interest in the product, and a *mere monetary interest* was not enough, even if the revenue was essential for tribal government operations. Finally, the Court would not agree that the state sales tax burdened Indian commerce because the non-Indian market for reservation cigarettes:

[E]xisted in the first place only because of a claimed exemption from these very taxes. The taxes under consideration do not burden commerce that would exist on reservations without respect to the tax exemption.

447 U.S. at 157.

2. *California v. Cabazon Band of Indians*, 480 U.S. 202 (1987). The doctrine of reservation-generated value was strengthened by the Supreme Court as a major barrier to the incursion of state authority in Indian reservations in *California v. Cabazon Band of Indians*. The Cabazon and Morongo Bands of Mission Indians occupy reservations in Riverside County, California. Because their reservations are small and without natural resources, the Bands adopted bingo ordinances, which were approved by the Secretary of the Interior, and began high-stakes bingo operations. The bingo facilities were constructed on tribal trust land with federal grants, and guaranteed loans under the Indian Financing Act of 1974, 25 U.S.C. §§ 1451 *et seq.*, and financial assistance from the Department of Housing and Urban Development and the Department of Health and Human Services.

Contrasting these circumstances with the facts of the cigarette tax cases, the Supreme Court noted that the Tribes built modern facilities to provide recreational activities and ancillary services to patrons who did not simply drive onto their reservations to make purchases and depart, but to spend extended periods of time enjoying services provided by the Tribes. The Court added that the Tribes have a strong incentive to provide comfortable, clean and attractive facilities and well-run games to increase attendance, and that the games were the sole revenue source for the Tribe and the major source of tribal employment. The Court found the Tribes' interests parallel to those of the federal government in supporting tribal economic self-determination. Accordingly, the Court found that state regulation of the bingo games would impermissibly infringe upon tribal self-government.

3. *Indian Country U.S.A. v. Oklahoma Tax Comm'n*, 829 F.2d 967 (10th Cir. 1987). Following the Supreme Court's lead in *Cabazon*, the Tenth Circuit Court of Appeals ruled in *Indian Country U.S.A.* that whenever an activity sought to be taxed by the state derives from reservation-generated value involving significant efforts of a tribe, a state will not be permitted to tax it. The court ruled that Oklahoma could not impose its sales tax on a bingo enterprise owned by the Creek Nation and managed under contract by Indian Country, U.S.A. Incorporated. The Tenth Circuit further found that, analogous to the *Cabazon* fact pattern, and unlike the cigarette tax cases, the value sought to be taxed derived solely from the Tribe's on-reservation efforts. The court rejected the state's argument that the legal and economic incidence of the sales

tax was on the non-Indian purchaser of services. Interestingly, the court even refused to allow the state to tax the sale of food, bingo supplies and accessories to non-Indian purchasers.

4. *Gila River Indian Community v. Waddell*, 967 F.2d 1404 (1992). The importance of the doctrine of reservation-generated value with respect to tribal economic development on tribal trust land is the basis of the Ninth Circuit Court of Appeals decision in *Gila River Indian Community v. Waddell*. The Gila River Reservation borders the City of Phoenix, Arizona. In order to foster tribal economic growth and provide tribal employment in the 1970s, the Tribe constructed Firebird Lake and the Sun Valley Marina on the Reservation wholly from federal funds. The Tribe then chartered Sun Valley Marina Corporation (Sun Valley) and leased it the Firebird Lake property. The lease was approved by the Secretary of the Interior pursuant to 25 U.S.C. § 415. Sun Valley subleased four pieces of land, including the lake, to a non-Indian partnership, Firebird International Raceway Park (Firebird), for boat and automobile racing. Firebird subleased a portion of the property to Compton Terrace for construction and operation of an amphitheater for the performing arts.

Arizona attempted to assess its transaction privilege tax of 5% on Sun Valley and Compton Terrace for on-reservation activities. The Tribe filed an action in the Arizona federal district court, seeking a declaratory judgment and seeking to enjoin the imposition of state taxes. The federal district court dismissed the case and the Tribe appealed to the Court of Appeals, which reversed. The Ninth Circuit began its legal analysis by pointing out that there is "no rigid rule" governing the attempts of states to tax non-Indians conducting business on Indian reservations, but emphasized that the case be assessed on the basis of the two independent barriers to state authority: (1) federal preemption, and (2) infringement upon tribal self-government.

The court then expounded upon the "particularized inquiry" test discussed above, weighing federal, state, and tribal interests to determine whether state interests are sufficient to justify the assertion of state authority. Central to such a particularized inquiry, the court noted, is the doctrine of reservation-generated value.

Beginning with federal interests, the Ninth Circuit pointed out that the sublease from Sun Valley to Firebird was approved by the Secretary of the Interior and required Firebird to construct boat-racing facilities, a drag strip and other automobile racetracks, bleachers for 15,000 people, picnic facilities, restrooms and concession stands. The lease provided that all improvements belong to the Tribe and required Firebird to pay the Tribe a sizeable annual base rent plus a graduated percentage of gross receipts and tribal taxes on sale of tickets and concessions. Firebird employs a number of tribal members.

The Ninth Circuit also pointed out that the sublease from Firebird to Compton Terrace was approved by the Secretary of the Interior and required Compton Terrace to construct a theater, restrooms and dressing facilities. The sublease provided that all improvements belong to the Tribe and required Compton Terrace to pay the Tribe a percentage of gross receipts of Compton Terrace performances and tribal taxes on sale of theater tickets, concessions and souvenirs. Compton Terrace employs a number of tribal members.

The Court then noted that the federal leasing statute, 25 U.S.C. § 415, establishes a federal regulatory scheme governing the leasing of tribal lands similar to that described by the Supreme Court in *Bracker* regarding the harvesting of Indian timber. Tribal land leases must be approved by the Secretary of the Interior under regulations requiring consideration of the uses to which the land will be put, the effect of such uses on neighboring tribal property, the availability of services appropriate to maintenance of such uses, the quality and safety of structures erected pursuant to the leases, the requirement of insuring the highest economic return to the Tribe consistent with prudent management and conservation practices, provisions regarding the length of leases and the terms of lease approval. The Ninth Circuit found the scope and detail of such a federal regulatory scheme sufficient to support a tribal argument that there exists no room for additional regulation by the state.

Turning to tribal interests in the Tribe's economic development, the Ninth Circuit noted that tribal involvement included the Tribe's working closely with Sun Valley and Compton Terrace to insure high-quality entertainment to the public; regulating and monitoring the property; enforcing tribal ordinances concerning water quality, pest control, sanitation and sewage disposal; limiting the size of audiences at performances; approving or rejecting additional construction; and coordinating law enforcement and security at events conducted on the reservation. The court noted that these tribal efforts, like those in *Cabazon*, involved activities characterized as reservation-generated value--auto and boat races, and theatrical and musical performances. In addition, the court noted that the Tribe alleged that its base rent, percentage of gross receipts, and tribal taxes would all suffer from imposition of the Arizona tax.

Because the case was dismissed without trial, Arizona did not show that the state provided any services with respect to any of the on-reservation activities, or that its taxes were "narrowly tailored" to fund any such state services. *See Crow Tribe of Indians v. Montana*, 819 F.2d 895, 900-902 (9th Cir. 1987) (*Crow II*), *summarily aff'd*, 484 U.S. 997 (1988). Finally, the Ninth Circuit pointed out that the doctrine of tribal self-government bears a resemblance to federal preemption, and concluded by holding that the Tribe is entitled to a trial in the case to prove that federal preemption and tribal self-government, taken together, prohibit the state tax. It is unlikely that, upon trial of the matter, the state will be able to meet its burden. Even in light of the fact that the case is not finally decided, it strongly reaffirms the importance of substantial tribal involvement in economic development on tribal trust lands on the reservation as a means of protecting the Tribe's tax immunity and preventing incursions of state taxing and other regulatory jurisdiction of the reservation.

5. *Salt River Pima-Maricopa Indian Community v. Arizona*, 50 F.3d 734 (9th Cir. 1995). Generating value on the reservation requires more than making leasing arrangements to use trust land and providing governmental services to non-Indian businesses. The Salt River Pima-Maricopa Indian Community established a shopping mall, known as the Scottsdale Pavilion, on individual allottees' trust land leased to a non-Indian land developer for a term of 55 years. The developer sublet the property to non-Indian businesses including Circuit City, Clothestime, Cost Plus Imports, Denny's, J.C. Penney, McDonald's, Taco Bell, Kentucky Fried Chicken and Home Depot. The Community collects a 1% tax on gross receipts from sales at the mall and provides police protection, some fire protection, health and safety inspection, zoning regulation and other services. The state collects sales and rental taxes from the subtenants and also provides services.

The Ninth Circuit Court of Appeals upheld the state taxes against the Community's challenge that they interfered with its right to impose taxes. The Court concluded:

[I]t is clear that the balance tips in favor of Arizona's taxation. Most importantly, the goods and services sold are non-Indian, and the legal incidence of Arizona's taxes falls on non-Indians. *See Colville*, 477 U.S. at 151 (*citing Moe*, 425 U.S. at 482). Furthermore, Arizona and its agents provide the majority of the governmental services used by these taxpayers. Consequently, the state's interest is at its strongest, not its weakest . . . .

If we were to disallow the state tax, there is nothing to prevent the Community from "open[ing] chains of discount stores at reservation borders, selling goods of all descriptions at deep discounts and drawing custom from surrounding areas." [*Colville*, 477 U.S.] at 155.

50 F.3d at 737-38. The Ninth Circuit carefully distinguished the situation in *Salt River* from that in *Gila River Indian Community v. Waddell*, above:
The Gila River Community maintained an active role in the business enterprise by developing and marketing on-reservation entertainment to the general public. . . .

Gila River is clearly distinguishable from this case. The mall earns its profits simply by importing non-Indian products onto the Reservation for resale to non-Indians. . . . [T]he businesses are managed and owned by non-Indians, and the Community does not participate in business decisions and does not share in the profits. Consequently, Gila River is more akin to cases in which state taxes are preempted because an Indian resource or service is being sold, which is not the case here.

50 F.3d at 738. In general, imported manufactured goods brought onto the Reservation for the purpose of resale by non-Indians to non-Indians will not meet the test for value generated on the Reservation. Entertainment and services provided to spectators and gamblers, or sale of natural resources of the Reservation, represent substantial value generated on the Reservation.

I. WHEN LEGAL INCIDENCE DETERMINES THE OUTCOME.

At times the aspect of legal incidence of the tax determines the outcome, as it did in *Oklahoma Tax Commission v. Graham*, 31 F.3d 964 (10th Cir. 1994), a case involving the Chickasaw Nation. The State of Oklahoma attempted to impose (1) beer tax on wholesale beer distributors selling beer to tribally operated stores in Indian country and (2) motor fuel tax on sales by tribal retail outlets of fuel to tribal members and non-Indians. But in the Oklahoma statutes the legal incidence of the beer tax was imposed on the wholesaler at the time of his purchase of the beer, not the retailer, the Chickasaw Nation. The statute provided that the wholesaler could only sell beer on which the tax had first been paid. On that basis alone the Tenth Circuit upheld the Oklahoma tax. But the Court added that because 18 U.S.C. § 1161 delegates liquor control to both tribes and states, Oklahoma clearly had the right to regulate beer sales in tribal outlets. Then the Court noted that the beer tax was not primarily a revenue raising measure, but a regulatory measure and did not even appear in the taxation code of the Oklahoma statutes, but in the liquor regulation section. Finally, the Court held the tax to be a valid regulatory measure.

To the argument of the Chickasaw Nation that the wholesalers could not legally shift the economic burden of the tax to the Nation, the Tenth Circuit pointed out that in *Seneca-Cayuga Tribe v. State ex rel. Thompson*, 874 F.2d 709, 715 (10th Cir. 1989), it held the sovereign immunity of a tribe to be co-extensive with that of the United States and further pointed out that the Supreme Court held in *South Carolina v. Baker*, 485 U.S. 505 (1988), that a nondiscriminatory tax imposed on a private entity that does business with the United States and passes the cost of that tax on to the United States does not violate federal sovereign immunity. Therefore, said the Tenth Circuit, the state tax is legal.

The Tenth Circuit's treatment of the Oklahoma fuel tax, however, was quite another matter. The Court noted that the sixteen cent per gallon fuel tax remittance procedure indicated the legal incidence of the tax to be clearly on the retailer, here the Chickasaw Nation. Even though the tax statute clearly contemplated that the economic burden of the tax be passed on to the retail purchaser, the Court held that imposition of the tax upon the Nation was preempted by federal law and struck the tax. Thus, the element of legal incidence of the tax proved fatal.

In *Oklahoma Tax Comm'n v. Chickasaw Nation*, 115 S. Ct. 2214 (1995), the United States Supreme Court upheld the Tenth Circuit's treatment of the Oklahoma fuel tax because the legal incidence of the tax rested on the Tribe. The Court noted that Oklahoma could accomplish its goal by declaring the tax to fall on the consumer and directing the Tribe to collect and remit it. *Id*. at 2221. The Tribe did not seek review of the lower court's ruling upholding the sales taxes on beer. *Id*. at 2218., n.3. (The Supreme Court also upheld Oklahoma's income tax on income of tribal members who work within Indian country but reside outside of it.)

J. WHEN LEGAL INCIDENCE IS IRRELEVANT.

An important aspect of *Gila River* was the need for the Tribe to show the economic incidence of the Arizona tax upon the Tribe itself. But legal incidence can become irrelevant when reservation-generated value is absent. For example, the legal incidence of Arizona's tax on cigarette sales was irrelevant in *State ex rel. Dept. of Revenue v. Dillon*, 826 P.2d 1186 (Ariz.App. 1991), because the Indian retailer on the Reservation was not a member of the Tribe. Harry Dillon, an enrolled member of the Puyallup Indian Tribe of Washington State, operated the Dillon Tobacco Barn inside the boundaries of the Tohono O'Odham Indian Reservation just outside Tucson, Arizona. Arizona attempted to levy and collect its luxury privilege tax upon Dillon's retail sales of cigarettes to nonmembers on the reservation.

To Dillon's claim that the state tax was invalid because it is specifically legally incident upon the retail cigarette seller, an Indian, the Arizona Court of Appeals pointed out that in the *Colville* case the Supreme Court equated "non-resident Indians" selling cigarettes on a reservation to "non-Indians", thus making the concept of legal incidence irrelevant. The Arizona Court bolstered its conclusion by pointing out that the only issue in *Warren Trading Post* was whether Arizona could validly tax proceeds of the Trading Post's Navajo Reservation sales to enrolled Navajo Indians. Finally, the Arizona Court held that even if the state's tax on Dillon's sales destroyed his business altogether and deprived the tribe of its 5% gross sales tax, nonetheless, the tax did not interfere with the right of reservation Indians to make their own laws and be ruled by them, citing *Colville*.

K. SHIFTING LEGAL INCIDENCE TO THE NON-INDIAN.

1. *Agua Caliente Band of Mission Indians v. County of Riverside*, 442 F.2d 1184 (9th Cir. 1971), *cert. denied*, 405 U.S. 933 (1972) and *Fort Mojave Tribe v. County of San Bernardino*, 543 F.2d 1253 (9th Cir. 1976), *cert denied*, 430 U.S. 983 (1977). *Agua Caliente* and *Fort Mojave* stand for the proposition that a *mere economic loss* suffered by a tribe as a result of a tax paid by a non-Indian alone is not sufficient to invalidate the state tax. *Agua Caliente* and *Fort Mojave* both upheld the California possessory interest tax on non-Indian lessees of Indian trust land. The possessory interest tax was a tax on possession of land by the non-Indian lessees. Therefore, the *legal incidence* of the tax was on non-Indians. Although there was an economic impact on the Indian tribe, the Ninth Circuit said in *Fort Mojave* that federal law did not preempt the possessory interest tax. The court said that before it would find the state tax preempted, it would need a strong indication from Congress that it wanted non-Indians to be immune from the tax. The court also said that the Tribe's right to govern itself (tribal sovereignty) was not violated by the tax because the tax would only have the indirect effect of "perhaps" reducing tribal revenues.

With great ease, the state can shift the *legal incidence* of a tax on reservation commerce from the Indian tribe or individual Indian to non-Indians. The California possessory interest tax, which was dealt with in *Fort Mojave* and *Agua Caliente,*is an excellent example of this shift of the legal incidence of a tax. The possessory interest tax might just as well have been a property tax, a tax on the tribe's *ownership* of its trust land. The two taxes would yield approximately the same amount of revenue because the possessory interest tax was based upon the value of the leasehold. But a property tax levied against the Tribe would have been unlawful because trust land is not subject to state property taxes. Therefore, in order to lay a tax on the value of the property, the state taxed the non-Indian lessee's *possession* of it.

By shifting the legal incidence of a tax from an Indian tribe or individual Indian to a non-Indian, the state makes it easier to defend the tax. An example of such a shifting is illustrated in *High Tide Seafoods v. State of Washington*, 106 Wn.2d 695, 725 P.2d 411 (1986). The tax at issue in *High Tide Seafoods* was a tax levied upon purchasers of fish. The statute provided that the purchaser could deduct one-half of the tax from the price paid to the seller. Indian treaty fishermen were exempt from the tax since the State cannot tax the exercise of a treaty right. Thus, under the statutory scheme, the purchaser of Indian treaty fish ended up paying a higher tax himself than he would have if he had bought fish from non-treaty fishermen. Although the tax ends up as a tax on the treaty-guaranteed fishing right, nonetheless, because the tax itself was imposed upon the purchaser rather than upon the Indian fishermen, it withstood a court challenge in the Washington Supreme Court. The end result is that fish purchasers shifted the economic burden to the treaty fishermen by lowering their purchase prices. Had the case been considered by the United States Supreme Court, it might well have been reversed.

Shifting the legal incidence of a state tax to non-Indians does not *guarantee* that it will be upheld as a valid tax. In *Central Machinery v. Arizona State Tax Comm'n*, 448 U.S. 160 (1980), when considering the transaction privilege tax which Arizona tried to impose on a non-Indian company selling farm machinery to an Indian tribe, the Supreme Court said:

Nor may [the State] distinguish the present case from *Warren Trading Post*. . . by contending that the tax at issue in this case falls upon the (non-Indian) seller of goods and not the (Indian) buyer because it is a tax on the privilege of doing business in Arizona rather than a sales tax. The tax in issue in the present case is precisely the same tax involved in *Warren Trading Post*. The argument made by [the State] in the present case was used by the Supreme Court of Arizona in *Warren Trading Post* to uphold imposition of the tax . . . . Our reversal of that decision recognized that, *regardless of the label placed upon this tax*, its imposition as to on-reservation sales to Indians could disturb and disarrange the statutory plan Congress set up in order to protect Indians against prices deemed unfair or unreasonable by the Indian Commissioner.

448 U.S. at 163 n.3 (emphasis added).

Thus, shifting the legal burden of a tax from an Indian tribe or individual Indians to non-Indians will not save the tax if it violates the federal preemption doctrine, Indian self-government or the Indian Commerce Clause.

L. STATE INCOME TAXES.

1. Taxation of Indian Income.

a. *McClanahan v. Arizona State Tax Comm'n*, 411 U.S. 164 (1973). In *McClanahan*, the Supreme Court held that the State of Arizona could not impose its personal income tax on a "reservation Indian" whose entire income was earned on the reservation. It said that by attempting to impose the tax, Arizona had interfered with matters, "which the relevant treaty and statutes leave for the federal government and for the Indians themselves." 411 U.S. at 179-180.

Almost the instant it was written, the *McClanahan* decision stood for a proposition which clearly went beyond its own limited facts and circumstances. In reaching its decision in *McClanahan*, the Supreme Court examined the Navajo Treaty, the Buck Act, the Arizona Enabling Act, and Public Law 83-280 as if those laws were particularly important factors in the decisions, and as if its decision would be different if any of those factors were absent or were in some way modified. The Navajo Treaty, of course, applies only to the Navajo Tribe and the Arizona Enabling Act would affect only Indian tribes in Arizona or tribes in states with similar enabling acts. So, one might think that *McClanahan* would be applied on a case-by-case basis, with each case turning on the particular circumstances of the tribe involved. But on the very same day that *McClanahan* was decided, the Supreme Court also decided *Mescalero Apache Tribe v. Jones*, 411 U.S. 145 (1973), which made *McClanahan* a general rule rather than merely a specific holding. In *Mescalero* the Supreme Court said:

[I]n the special area of state taxation, absent cession of jurisdiction or other federal statutes permitting it, *there has been no satisfactory authority for taxing Indian reservation lands or Indian income from activities carried on within the boundaries of the reservation*, and *McClanahan v. Arizona State Tax Comm'n, supra*, lays to rest any doubt in this respect by holding that such taxation is not permissible absent congressional consent.

411 U.S. at 148 (emphasis added).

This rule apparently does not depend on the particular treaty covering a reservation, or the state enabling act, or the other laws which were considered in *McClanahan*. Rather, it deals with a key issue in state Indian tax questions: where is the *legal incidence* of the state tax? If the legal incidence of the tax falls on a reservation Indian who earns income on the reservation and who resides on the reservation the tax will fail. However, if either of the two elements is missing, the matter is less than certain. On the other hand, if both elements are missing, that is, if the Indian earns income off the reservation and resides off the reservation, the tax will succeed.

The breadth of *McClanahan* is illustrated by *Eastern Band of Cherokee Indians v. Lynch*, 632 F.2d 373 (4th Cir. 1980). The Fourth Circuit Court of Appeals held that the State of North Carolina could not tax the reservation income of members of the Eastern Band in spite of the facts that the state had a history of exercising jurisdiction over the Band and that title to the Band's reservation was originally obtained by grant from the state.

b. Geographical Component. Clearly, the "legal incidence" rule stated above incorporates another important factor in state Indian tax considerations: the "geographical component." The presence of the subject or activity being taxed *within the reservation* was an important element in the *McClanahan* decision. Today, the "geographical component" is still one of the first reference points used by courts in determining the scope of state and tribal powers.

In the absence of the geographical component, that is, when an Indian earns income off the reservation and resides off the reservation, his income is subject to state income tax. This flows naturally from the Supreme Court's statement in *Mescalero* that "[a]bsent express federal law to the contrary, Indians going beyond reservation boundaries have generally been held subject to non-discriminatory state law otherwise applicable to all citizens of the state." 411 U.S. at 148. Citing the quoted statement, the appellate court in New York held, *In the Matter of Mark D. George v. Tax Appeals Tribunal*, 548 N.Y.S.2d 66 (A.D. 3 Dept. 1989), that an enrolled Onondaga Indian living off the reservation and working off the reservation was subject to New York's income tax.

c. *Bryan v. Itasca County*, 426 U.S. 373 (1976). In *Bryan*, the Supreme Court refined *McClanahan* by holding that even states which had civil jurisdiction over Indian reservations under Public Law 83-280 were without authority to tax reservation Indians. It said that Public Law 83-280 did not give states *regulatory* or *taxing* jurisdiction over Indian reservations.

d. The Scope of *McClanahan*: Who Are "Reservation Indians?" Since McClanahan herself was a Navajo Indian residing on the Navajo Reservation, the *McClanahan* decision left unanswered at least two other questions besides those mentioned above. They are discussed below:

(1) Does "reservation Indian" mean only an Indian residing on a reservation? This question has been at least partly answered in the affirmative. It appeared in 1992 that the term "reservation Indian" meant an enrolled tribal member of the reservation in question, whether he resides on or off the reservation. In *Sac and Fox Nation v. Oklahoma Tax Comm'n*, 967 F.2d 1425 (10th Cir. 1992), Oklahoma attempted to levy a state income tax on earnings of tribal members who

worked on tribal trust land which was not officially designated as a reservation. The district court struck down the tax on the basis of the *McClanahan* rule but made no effort to determine the place of residence of the tribal members involved.

On appeal, the Tenth Circuit Court of Appeals began its legal analysis of the issue by pointing out that direct state taxation of tribal property, or tribal income earned on a reservation, is presumed to be preempted absent an express congressional authorization, citing *McClanahan* and *Mescalero*. The court then underscored that trust land is equivalent to a reservation for tribal tax immunity purposes, citing *Oklahoma Tax Comm'n v. Potawatomi Indian Tribe*, 111 S.Ct. 905 (1991). Finding no express congressional authorization for the imposition of state income taxes, the court struck down the state's income tax on tribal employees, regardless of their residence on or off the reservation. Because the court found residence of tribal members irrelevant, it did not remand the case to the trial court for a determination of where the tribal members in question lived. The court's logic seemed impeccable given that the Supreme Court in *Mescalero* tied Indian tax immunity to "activities carried on within the boundaries of the reservation" and not to the residence of the Indian wage earner. 411 U.S. at 148.

The matter became much less certain with the Supreme Court's decision upon appeal in *Oklahoma Tax Comm'n v. Sac and Fox Nation*, ___U.S. ___, 113 S. Ct. 1985 (1993). The Supreme Court affirmed the presumption that Oklahoma may not tax the income of Sac and Fox tribal members who live and work on the Reservation, but reversed the lower court and ruled that, upon remand, the residence of the tribal members is important to the final determination of taxability of their income. The Court said, rather cryptically:

If it is determined on remand that the relevant tribal members do live in Indian country, the Court of Appeals must analyze the relevant treaties and federal statutes against the backdrop of Indian sovereignty. Unless Congress expressly authorized state tax jurisdiction in Indian County, the McClanahan *presumption* counsels against finding such jurisdiction.

113 S. Ct. at 1986. (emphasis added).

The Supreme Court's use of language is troubling. Why, for instance, did the Supreme Court not invoke the per se rule from *Cabazon*? Why did the Court refer to the *McClanahan* principle as a "presumption"? Analysis of *McClanahan*reveals no discussion of a "presumption" against state taxation. Rather, the Supreme Court held straightforwardly that a state may not tax income earned by an Indian who lived and worked on the Navajo Reservation without specific authorization from Congress. Does this newly-coined "presumption" mean that the Supreme Court is starting down the slippery slope toward allowing states to tax Indian income? The answer to that question is probably "yes."

In *Oklahoma Tax Commission v. Chickasaw Nation*, 115 S. Ct. 2214 (1995), the Supreme Court reversed the Tenth Circuit Court of Appeals and upheld a state income tax on tribal members employed by the Nation in Indian country but residing outside of Indian country. Importantly, the Tribe had not asserted that the state's tax "infringes on tribal self-governance." *Id*. at 2223. Instead, the Tribe's argument was based on the Treaty of Dancing Rabbit Creek, in particular, the following language:

...no Territory or State shall ever have right to pass laws for the government of the [Chickasaw] Nation or Red People and their descendants...but the U.S. shall forever secure said [Chickasaw] Nation from, and against, all laws except such as from time to time may be enacted in their own National Councils, not inconsistent with the Constitution, Treaties, and Laws of the United States . . . .

7 Stat. 333. Because the Treaty clearly prohibited Oklahoma from passing laws for the government of the Chickasaw or their descendants, the Tenth Circuit held the question of residence irrelevant and the State's tax power preempted. However, by a five to four vote, the Supreme Court held that the Treaty language only provided for the Tribe's sovereignty within Indian country, stating:

We do not read the Treaty as conferring supersovereign authority to interfere with another jurisdiction's sovereign right to tax income, from all sources, of those who choose to live within that jurisdiction's limits.

Id. at 2224. Justices Breyer, Stevens, O'Connor and Souter believed the Treaty language fit the tax at issue and reminded the Court that if the language might refer to Chickasaw lands west of the Mississippi on the one hand, or Indian country on the other hand, that the ambiguity should be construed in favor of the Indians.

At least two courts had already decided off-reservation residence questions against Indians. The United States District Court for the District of Montana in *Dillon v. Montana*, 451 F. Supp. 168, *rev'd* 634 F.2d 463 (9th Cir. 1978), held that a state can impose its income tax on an Indian who works on the reservation but resides off. It said that residency on the reservation is a requirement for bringing an Indian under the coverage of *McClanahan*, 411 U.S. 164 (1973), because *McClanahan* is based upon territorial principles. It said that if the Indian lives off the reservation, that is the *situs* of his income even if he earns it on the reservation, and therefore the state tax is actually imposed off the reservation.

Although *Dillon* was reversed on appeal on completely different grounds, the Supreme Court of Wisconsin adopted the reasoning of *Dillon* in *Anderson v. Wisconsin Dept. of Revenue*, 484 N.W.2d 914 (Wis. 1992). Anderson, an enrolled member of the Lac Courte Oreilles Band of Lake Superior Chippewa Indians, was employed by the Tribe as high school guidance counselor, director of education and later president of the Lac Courte Oreilles Community College. During such employment, however, Anderson lived off the reservation. The State of Wisconsin held that the term "reservation Indian", as used in *McClanahan*, referred only to an Indian living on the reservation and noted that Wisconsin law provided that "all income of resident individuals follows the residence of the individual." *Id.* at 916. Before upholding the state income tax, however, the Wisconsin Supreme Court conducted a particularized inquiry into federal, state, and tribal interests, and concluded that Wisconsin's income tax was not preempted by federal law. Nor did the tax interfere with tribal self-government in the absence of any showing that the economic incidence of the tax would be passed on to the Tribe.

The *Anderson* decision seemed, upon close analysis, to be wrong for several reasons: first, on the same day on which it handed down *McClanahan*, the Supreme Court stated in *Mescalero* that "there has been no satisfactory authority for taxing Indian reservation lands *or Indian income from activities carried on within the boundaries of the reservation* . . . ." 411 U.S. at 148 (emphasis added). It is true that Mrs. McClanahan was a resident of the Navajo

Reservation and that the Supreme Court did not define its term "reservation Indian," but the *Mescalero* opinion seems to make it clear that the derivation of income from on-reservation activities is the deciding factor; therefore, Wisconsin's attempt to justify its income tax, by statutorily establishing the *situs* of Anderson's income as at his residence off the reservation, seems contrary to the *Mescalero* holding.

In *LaRoque v. State*, 583 P.2d 1059 (Mont. 1978), the Supreme Court of Montana held "that *situs* of the activity is the primary factor in determining whether state taxation jurisdiction exists . . . the important factors were the coalescence of*situs* (reservation) and status (Indian)" *id.* at 1064. It concluded that Montana could not tax income earned on a Montana reservation by a nonmember Indian. Since state law does not apply within a reservation without a specific delegation of jurisdiction by Congress, the reasoning of the Montana Supreme Court appears consistent with the *Mescalero* holding.

A variation of this question was decided by the Montana Supreme Court in *State Dept. of Revenue v. Bird*, 829 P.2d 941 (Mont. 1992). Adrian Bird was an enrolled Crow Indian who resided within the boundaries of the Crow Reservation but mined coal, which was held in trust for the Crow Tribe by the United States, in a ceded strip of land adjacent to but outside the Reservation. Montana attempted to tax Mr. Bird's income. The Montana Supreme Court, noting that the Ninth Circuit Court of Appeals had determined the tribal trust coal to be "a component of the reservation land itself," *Crow Tribe v. Montana*, 650 F.2d 1104, 1117 (amended 1982), 665 F.2d 1390, *cert. denied*, 459 U.S. 916 ("*Crow I*"), by virtue of a 1958 congressional act, Act of August 14, 1958, 72 Stat. 575, held that the Montana income tax did not apply. Thus, while Mr. Bird worked outside the Reservation in terms of physical boundaries, the Montana Court felt that he worked on the Reservation in the sense that he was mining reservation coal. The outcome, however, appears not to have changed Montana's basic rule that reservation residence is required to protect an enrolled Indian from state income tax no matter where he earns his income.

(2) Is an Indian who is not a member of the tribe on whose reservation he resides a "reservation Indian" for purposes of the rule that a state tax may not be imposed upon the income of a "reservation Indian" earned on the reservation? Lower court cases have answered this question differently. The Minnesota and Montana Supreme Courts have held, respectively, in *Topash v. Commissioner of Revenue*, 291 N.W.2d 679 (Minn. 1980), and in *LaRoque v. State* (1978), that even an Indian who lives on another tribe's reservation is immune from state taxes on income earned on that reservation. In *Topash*, the Court noted that in *McClanahan* the Supreme Court had used the term "reservation Indians" to designate Indians who are exempt from state taxes, even though it was dealing in that case with an enrolled Navajo Indian residing on the Navajo Reservation. It also reviewed several federal statutes, which refer to Indians generally without distinguishing among them on the basis of tribal affiliation and found that the statutes express a broad general policy of protecting "Indians, of whatever tribe, from state government interference." Given this background, the Minnesota Supreme Court reckoned that since no federal statute expressly authorizes such taxation the question ought to be resolved in favor of Indians.

In *LaRoque*, the Montana Supreme Court examined federal and state court decisions on the issue of state jurisdiction over Indian reservations. The court concluded that the situs (location)

of the activity and the subject matter of the activity were more important in determining whether the state has jurisdiction than the enrollment of the person involved. In earlier cases, the federal courts have clearly denied the State's authority over Indians on reservations even though they were not enrolled in the tribes occupying those reservations.

The same result was first reached by the New Mexico Supreme Court in *Fox v. Bureau of Revenue*, 531 P.2d 1234 (N.M. 1975), *cert. denied*, 424 U.S. 933 (1976), but has since been reversed in *New Mexico Taxation and Revenue Department v. Greaves*, 864 P.2d 324 (1993). The New Mexico Court noted that the Supreme Court has explained that the *McClanahan* rationale does not apply to taxation of *nonmembers*, even when they are Indians. Accordingly, the New Mexico Court overruled *Fox.*

The Federal Bankruptcy Court for the District of Arizona reached a similar result in *In Re Carmen Smith and Merrenda Smith, Debtors*, 158 B.R. 818 (1993).

2. Taxation of Non-Indian Income. The Buck Act, 4 U.S.C. § 106, is a federal law which permits states to tax the income of people living within federal areas. Indian reservations are federal areas, but Indians "not otherwise taxed" are expressly exempted from the coverage of the Buck Act. The intent of this Act may have been to allow state taxation of non-Indians on Indian reservations, but this intent is not entirely clear.

3. Summary and Comment. The result of *McClanahan*, *Mescalero*, *Chickasaw*, and other cases is the general rule that whenever the *legal incidence* of a state tax would fall on a reservation Indian engaging in activity on the reservation or on an Indian tribe operating within the reservation, the state tax must fall.

M. STATE CORPORATIONS: DANGEROUS PITFALLS.

As a general rule, a corporation is a legal personality, separate from its owners. Therefore, a danger exists when a tribe forms a business corporation under state law. It is possible it may lose the benefit of its Indian tribal status for state tax purposes.

1. *Eastern Navajo Industries v. New Mexico Bureau of Revenue*, 552 P.2d 805 (N.M. 1976). The argument that state taxation of an Indian-controlled state corporation interferes with Indian self-government has been successfully argued in the State of New Mexico. In that case, the tribal council formed a corporation with the help of federal funds from the Indian Business Development Fund. A majority of the stockholders were Indians. The New Mexico Supreme Court said that sales taxes could not be imposed on this corporation, even though it was formed under state law. Under the Indian Business Development Fund Act, a corporation can be considered an Indian corporation if at least 51% of the stock is owned by an Indian tribe or Indians. Since the corporation was an Indian corporation under this act, the court gave it the same tax status as an Indian tribe.

2. *United States v. Tax Comm'n of Mississippi*, 535 F.2d 300 (1974). In *United States v. Tax Comm'n of Mississippi*, the federal government brought suit on behalf of the Mississippi Band of Choctaw Indians to enjoin the Mississippi State Tax Commission from imposing a sales tax on a

tribal construction company, Chata Development Company, a state-chartered corporation, doing business on the Choctaw Indian Reservation. The Fifth Circuit Court of Appeals upheld the state's tax, resting its decision on two grounds. First, the court held that under the Treaty of Dancing Rabbit Creek, 7 Stat. 333 (1830), the Mississippi Choctaws lost their status as a federally-recognized tribe, their reservation lost its status as an Indian reservation, and the Indians lost their immunity from state regulation. Second, the court noted that a state always has authority to tax state-chartered corporations because they are separate entities from the people who own them.

The validity of these holdings may be undermined altogether by the decision of the United States Supreme Court in *United States v. John*, 437 U.S. 634 (1978), in which the Supreme Court held that the Mississippi Choctaw Tribe had not lost its status as a federally-recognized tribe living on a federal Indian reservation and organized under the Indian Reorganization Act of 1934. However, at least in Mississippi, this case may still stand for the proposition that a state-chartered corporation, even owned 100% by a federally-recognized Indian tribe, is subject to state tax upon business performed wholly inside the reservation.

The holding of the New Mexico Court would seem to be more in keeping with federal policy inasmuch as the Small Business Act, the Indian Self-Determination and Education Assistance Act and the Indian Revolving Loan Fund Act, all classify a corporation owned 51% by Indians or Indian tribes as an "Indian entity" entitled to special federal benefits. Nevertheless, using a state-chartered corporation form is still risky from a tax standpoint because courts in other states may not follow the New Mexico Supreme Court's decision in *Eastern Navajo Industries*, 552 P.2d 805 (N.M. 1976).

N. TRIBALLY-CHARTERED CORPORATIONS.

Indian tribes possessing sovereign powers clearly have the authority to charter corporations. There does not appear to be any authority on the question of whether a state can tax a tribally-chartered corporation doing business on the reservation. Significantly, courts usually look to the law of the government which created the corporation to answer questions about its status. Accordingly, some tribes have enacted tribal corporations codes which provide that tribally-chartered corporations hold the same privileges and immunities from state interference as their stockholders possess. Such laws should be sufficient to stop attempts by states to tax or regulate the on-reservation activities of the corporation, but are not likely to prevent attempts by states to tax or regulate off-reservation activities. Remember that in *Mescalero Apache Tribe v. Jones*, 411 U.S. 145 (1973), the Supreme Court held that whenever an Indian tribe does business off the reservation, its gross receipts are subject to state tax the same as non-Indians. It is likely that the courts would hold that a tribally-chartered corporation, even if 100% tribally owned, possesses no greater tax immunity than the tribe itself.

O. STATE TAXATION OF NONMEMBER INDIANS.

The basic principle that states may not generally tax Indians living on reservations for on-reservation activities would seem logically to apply equally to members of the tribe on whose reservation the activity takes place, and to nonmember Indians living on the reservation.

In *Colville Confederated Tribes v. Washington*, 447 U.S. 134 (1980), the Yakima Indian Tribe, one of the plaintiffs in the case, litigated that issue with respect to state sales tax. The Supreme Court upheld the state sales tax on nonmember Indians, saying that even the broadest reading of federal statutes cannot be said to preempt state tax power upon nonmember Indians living on a reservation. The Court further said that while nonmember Indians come within the definition of "Indian" for purposes of the Indian Reorganization Act, that fact does not demonstrate a congressional attempt to exempt those nonmembers from state taxes.

Finally, the Court added that allowing state taxes on nonmember Indians does not contravene the principle of tribal self-government because the nonmembers are not constituents of the governing tribe. Referring to the "particularized inquiry" test, the Court concluded that the state's interest in taxing nonmember Indians outweighs any competing tribal interest. The principle of this case has now been extended to Oklahoma's vehicle taxes for nonmembers of the Sac and Fox Nation whose automobiles are principally garaged on tribal trust lands but used both on and off such lands. It has also been extended to Montana's new car tax and motor vehicle property tax for nonmembers of the Assiniboine and Sioux Tribes of the Fort Peck Reservation in Montana, discussed below.

P. STATE TAXATION OF INDIAN PROPERTY.

1. Personal Property.

a. The General Rule. In *Moe v. Confederated Salish & Kootenai Tribes*, 425 U.S. 463 (1975), the Supreme Court held that a state cannot impose a tax on the personal property of Indians on the Flathead Indian Reservation. Some of the Indians on the reservation lived on fee lands, lands no longer held in trust by the United States. The Supreme Court said that it did not matter whether the personal property was located on Indian trust land or fee land--it was all exempt from taxation. The Court said that the State of Montana had no jurisdiction over Indians within the reservation as long as the reservation still existed. It said that state jurisdiction did not depend on the ownership of particular parcels of land because that would result in "an impractical pattern of checkerboard jurisdiction."

b. Motor Vehicles. Later, in *Confederated Tribes*, the Supreme Court held that a state may not collect an excise tax levied upon Indian-owned vehicles and mobile homes based on the reservation, even though the motor vehicles were used partly off the reservation. Until recently it was felt by most authorities that the exemption of Indians for vehicle excise taxes required the original purchase of the vehicle to be made and completed inside the reservation. However, in *Assiniboine and Sioux Tribes v. Montana*, 568 F. Supp. 269 (D. Mont. 1983), a federal court in Montana held that there is no territorial component to Montana's new car tax which is imposed as a precondition to use of Montana highways and, therefore, the place of purchase of the new car is not a legitimate and valid element of the Indian tax exemption. The court invited Montana to offer additional evidence and legal argument on the matter; no further action on the case has been reported.

In *Sac and Fox Nation v. Oklahoma Tax Comm'n*, 967 F. 2d 1425 (1992), the Tenth Circuit Court of Appeals considered Oklahoma's attempt to tax motor vehicles owned by tribal members

on trust land not officially designated as a reservation, and used both on and off the trust land. Oklahoma imposed two motor vehicle taxes: the first was a vehicle excise tax, of 3 1/2% of the value of the automobile, imposed upon the transfer of legal ownership of the automobile; and the second was an annual registration fee imposed upon every vehicle using any public roads in Oklahoma. The Tribe itself issued tribal licenses to tribal members and levied a tax upon ownership, by tribal members, of motor vehicles principally garaged on tribal trust land. As could be expected, Oklahoma took the position that Sac and Fox tribal members enjoyed no tax immunity since their trust land was not designated a reservation.

By requiring, as a prerequisite to issuance of an Oklahoma certificate of title and license plate, that any purchaser of a vehicle previously tagged by the Tribe pay "back" motor vehicle taxes for the entire previous period during which the vehicle was tribally tagged, the state intended to shift the legal incidence of the tax to the motor vehicle itself. The Tenth Circuit found this ploy invalid for the obvious reason that it burdened tribal members by diminishing the fair market value of their automobiles upon resale and thus, the tax constituted a blatant attempt to do indirectly what it could not do directly. Accordingly, the Court struck the state's attempt to collect back taxes. The Court also noted that the annual registration tax could not stand in the absence of state evidence to show that it was "tailored" to the amount of use of their automobiles by tribal members off tribal trust lands. However, the Court did uphold the Oklahoma taxes upon nonmember owned vehicles on tribal trust land, citing *Colville*, and noting that the Tribe failed to show how imposition of such taxes would frustrate tribal self-government.

When the case reached the U.S. Supreme Court it first settled the reservation versus trust land problem by holding that:

The residence of a tribal member is a significant component of the McClanahan presumption against state tax jurisdiction. But our cases make clear that a tribal member need not live on a formal reservation to be outside the State's taxing jurisdiction; it is enough that the member live in "Indian country."

113 S. Ct. at 1991.

With respect to Oklahoma's vehicle taxes, the Supreme Court affirmed the Tenth Circuit, holding that:

Oklahoma's taxes are no different than those in *Moe* and *Colville* . . . . Oklahoma may not avoid our precedent by avoiding the name "personal property tax" here any more than Washington could in *Colville*.

113 S. Ct. at 1993.

c. The Community Property Problem. In *Makah Indian Tribe v. Clallam County*, 73 Wn.2d 677 (1968), the Washington Supreme Court held that Clallam County could not levy a personal property tax against a motel building, furniture, equipment, and rental boats on the reservation owned by a tribal member married to a non-Indian husband. The county argued that under the state community property law the non-Indian owned half of the property. Tribal custom, however, did not follow community property law. Under tribal custom, the Indian's property remained Indian even though the non-Indian's income contributed to the building of a new motel

and a new cafe and all new furnishings. The Court held that tribal custom controlled inside the reservation and the state's community property did not apply.

2. Land.

a. Trust Land. Tribal and individual Indian land which is held in trust by the United States is clearly exempt from state taxation.

b. Tribally-Owned and Indian-Owned Fee Land Inside a Reservation. Prior to the decisions discussed below, it could be forcefully argued that tribally-owned fee land inside a reservation should be exempt from state taxation. First, the taxation of tribal fee land by the state would certainly interfere with tribal self-government in violation of the principles laid down by the Supreme Court in *Williams v. Lee*, 358 U.S. 217 (1959). Second, early Supreme Court cases hold against the power of states to tax tribal lands. *See, e.g., The Kansas Indians*, 72 U.S. (5 Wall.) 737 (1866). Third, 25 U.S.C. § 177 prohibits the transfer of tribal land without consent of the United States. If a state had authority to tax tribal land it would also claim authority to seize it in payment of the tax. Such an action would clearly violate 25 U.S.C. § 177. The following cases, however, seriously undermine the effectiveness of these protections.

(1) *County of Yakima v. Yakima Indian Nation*, 502 U.S. 251 (1992). Whether tribally-owned and Indian-owned fee land inside a reservation is subject to state taxation may well depend upon whether the land was allotted pursuant to the General Allotment Act or another scheme, such as that established by the Treaty with the Omaha Tribe. This conclusion stems from *County of Yakima v. Yakima Indian Nation*, 502 U.S. 251 (1992), which involved an attempt by the State of Washington to levy real estate taxes and sales taxes on fee-patented, former trust allotments inside the Yakima Reservation and owned by the Yakima Tribe and enrolled tribal members. The Supreme Court upheld the real estate tax but struck down the sales tax in a very complicated opinion which hinges on what the Supreme Court found to be *a clearly manifested intention by Congress to permit the state tax*. To understand the decision, two sections of the General Allotment Act must be analyzed. Section 5 reads, in pertinent part, as follows:

[A]t the expiration of said [trust] period the United States will convey [the allotted lands] by patent to said Indian . . . in fee, *discharged of said trust and free of all charge or incumbrance whatsoever*. . . . And if any conveyance shall be made of the lands set apart and allotted as herein provided, or any contract made touching the same, before the expiration of the time above mentioned, such conveyance or contract shall be absolutely null and void. . . .

25 U.S.C. § 348 (emphasis added). Section 6 of the General Allotment Act, *as amended by the Burke Act,* Burke Act of 1906, 34 Stat. 182, reads in pertinent part as follows:
At the expiration of the trust period and when the lands have been conveyed to the Indians by patent in fee, . . . then each and every allottee shall have the benefit of *and be subject to* the laws, both civil and criminal, of the State or Territory in which they may reside. . . . *Provided*, That the Secretary of the Interior may, in his discretion, and he is authorized, whenever he shall be satisfied that any Indian allottee is competent and capable of managing his or her affairs at any time to cause to be issued to such allottee a patent in fee simple, *and thereafter all restrictions as to sale, incumbrance, or taxation of said land shall be removed.*

25 U.S.C. § 349 (emphasis added).

Section 6 was considered by the Supreme Court in *Moe*; the Court said that the state did not have taxing jurisdiction *even* over Indians living on fee patented lands. The Court based this conclusion on the policy of the General Allotment Act, which it said:

[W]as to continue the reservation system and the trust status of Indian lands, but to allot tracts to individual Indians for agriculture and grazing. *When all the lands had been allotted* and the trust expired, the reservation could be abolished.

425 U.S. at 479 (emphasis added). *Quoting Mattz v. Arnett*, 412 U.S. 481 (1973).

A close reading of the *Moe* opinion indicates that the Court understood this to mean that a reservation would not be abolished until *all* lands on the reservation had been allotted and the trust expired. Only then would Indians and their property be subject to general state jurisdiction, including taxing jurisdiction; but so long as trust land existed within a reservation, its reservation status continued, and the state lacked jurisdiction over Indians *or their property anywhere on such reservation*unless jurisdiction were expressly given to it by Congress. That is to say, the *Moe* opinion seemed to hold that section 6 of the General Allotment Act is not an express grant of jurisdiction even over Indian-owned fee land in a reservation.

In keeping with the foregoing rationale, in *Battese v. Apache County*, 630 P.2d 1027 (Ariz. 1981), the Arizona Supreme Court held that Indian-owned fee lands within the Navajo Reservation are not subject to state property taxes. It reasoned that *McClanahan*, and other United States Supreme Court decisions, have made it clear that states simply do not have any justification for taxing Indian income or property located within reservation boundaries, regardless of the trust or fee status of the property.

However, in *Yakima Nation*, the Supreme Court changed its mind. The Court pointed out that *In re Heff*, 197 U.S. 488 (1905), held that the congressional purpose of section 6 of the Act was to make every allottee immediately subject to all state civil and criminal laws, but that Congress had changed that rule in the Burke Act by postponing subjection of allottees to state civil and criminal law until they received fee patents, and by adding the proviso removing tax immunity of the land upon "premature patenting"--that is, issuance of a fee patent to an allottee prior to expiration of the 25-year trust period. The Supreme Court emphasized the effect of the Burke Act proviso as not subjecting the *Indian allottee* to state civil and criminal law, but, instead, subjecting the *land* to state civil law, including tax law.

The Supreme Court found that language to be a clear intention by Congress to permit the state to tax Indian-owned fee land inside the reservation. The Court attempted to distinguish its change of heart against Indian tax immunity by characterizing the *Moe* opinion as focusing on the personal jurisdiction of Indian fee land owners on the reservation rather than on the land itself. The Court concluded that because the state's tax jurisdiction is upon the land, rather than upon the individual Indian, it is "assuredly not *Moe*-condemned . . ." as undesirable checkerboard jurisdiction, and that the parcel-by-parcel determinations of the state tax assessor on the reservation are essentially the same as those off the reservation, which take account of immunities of federally-owned, state-owned, and church-owned lands.

The Yakima Nation argued that the language of section 6, and earlier court decisions interpreting it, were modified by later statutes and court decisions. The Tribe argued that:

1) The Indian Reorganization Act of 1934 repudiated the policy of the General Allotment Act and extended the trust period indefinitely.

2) The Supreme Court decision in *Moe* that section 6 did not authorize Montana taxation of cigarette sales and personal property on fee lands, was based upon the rationale that if the General Allotment Act granted the state jurisdiction over Indians on fee patent lands, the Flathead Reservation would effectively be diminished in size.

3) 18 U.S.C. § 1151 defines "Indian Country" to include fee patent lands within Indian reservations.

The Yakima Nation's arguments were sound and should have held the day. Indeed, in his dissent, Justice Blackmun expressed his dismay at the Court's finding an "unmistakably clear" intent of Congress to allow states to tax Indian-owned, fee-patented lands from the Burke Act proviso. Justice Blackmun described the proviso as "now orphaned" because the Indian Reorganization Act of 1934 prohibited further allotments and extended the trust period indefinitely, and because Congress's extension of the federal criminal code to all Indian country, including fee-patent lands in 18 U.S.C. § 1151, essentially repealed the jurisdiction transfer embodied in section 6 of the General Allotment Act. Justice Blackmun also noted that the Court rigidly refused to construe the effect of the General Allotment Act in light of "intervening legislative enactments", although the Court had readily done so in *Bryan v. Itasca County* and in *Moe*.

Justice Blackmun underscored the fact that even the majority admitted that section 5 of the General Allotment Act only "implied" that the release of trust land from trust restrictions indicated congressional intent that it be subject to state taxation. Finally, Justice Blackmun expressed dismay at the majority's notion that it would be "strange" for Congress to release land from restrictions against alienation, but not, at the same time, subject it to state taxation. Justice Blackmun points out that such a notion conflicts with the principle that Congress has acted consistently upon the principle that states have no power to regulate the affairs of Indians on reservations, citing *Williams v. Lee*.

Turning to the sales tax on fee land in the reservation, the majority of the Supreme Court returned to the true principles of Indian tax immunity. Citing *Cabazon*, the Court noted that it has traditionally followed "a per se rule" in the special area of state taxation of Indian tribes and tribal members and pointed out that the rule both categorically prohibits state taxes in the absence of a federal grant of jurisdiction to the state and categorically allows such a tax when it has been authorized by Congress. Then, relying upon the rule that ambiguous provisions in Indian statutes are to be construed liberally in the Indians' favor, the Court noted that the precise language in the Burke Act proviso was "taxation of . . . land." Adding to this the Washington Supreme Court's observation that the state sales tax on land is not a tax on the land itself, the Supreme Court concluded that Congress had not authorized the sales tax and struck it.

The *Battese* decision, which holds that Indian-owned fee lands within the Navajo Reservation are not subject to state property tax, should still be good law. The reason is that trust allotments were never made on the Navajo Reservation under the General Allotment Act of 1887; thus, in *Battese*, there was no statute consenting to state taxation. The land in question was purchased by Indians after it had been patented to a non-Indian before the reservation was enlarged by Congress to include the land. The Arizona Supreme Court, relying on the rule established in *McClanahan* that federal preemption, read against the backdrop of Indian sovereignty, exempts reservation Indians from state taxes, held that:

[t]he property's status as trust, non-trust, and/or fee-patent land, is not determinative of the property's status as exempt from state taxation. The exemption applies if the subject property is owned by enrolled Navajo tribal members and is located within the present physical boundaries of the Navajo Reservation."

630 P.2d at 1029.

Thus, whenever an Indian owns fee land within a reservation which was never allotted under the General Allotment Act, as in the case of *Battese*, the Supreme Court's holding in *Yakima Nation* would not apply and the reasoning of *Battese*should prevail. Determination of whether Indian-owned fee land in a reservation is taxable requires an analysis of the particular statute which led to the land's becoming fee land; if such statute does not include a congressional grant of tax jurisdiction to the state, an attempted state tax should be defeated.

(2) *Lummi Indian Tribe v. Whatcom County, Washington*, 5 F.3d 1355 (1993), *cert. denied*, ___U.S.___, 62 USLW 3757 (1994). It begins to appear, however, that such is not to be the case, at least not in the Ninth Circuit Court of Appeals. That court considered the question of state taxability of four parcels of former trust land inside the Lummi Reservation purchased by the Tribe in fee status. When Whatcom County assessed ad valorem property tax against the parcels, the Tribe filed suit in the federal district court, seeking a declaratory judgment that the tax violated the Tribe's tax immunity. Because allotments were made to Lummi tribal members not pursuant to the General Allotment Act, but pursuant to the Treaty of Point Elliott, under the Supreme Court's reasoning in *Yakima Nation*, taxability of the land should have turned on whether the Treaty of Point Elliott indicated *a clearly manifested intention by Congress to permit the state tax*.

However, the Ninth Circuit held, in a 2-1 opinion, that:

In *Yakima Nation*, the Court found an unmistakably clear intent to tax fee-patented land. It did not rely on section 6 of the General Allotment Act as Yakima County proposes, concluding instead that the land's alienable status determines its taxability . . . . The Court made no distinction between fee land allotted by treaty and that allotted under the Act. Its interpretation of section 5 of the Act and the proviso to section 6 imply that no matter how the land became patented, it is taxable once restraints against alienation expire.

5 F.3d at 1357.

In these conclusions, the Ninth Circuit Court is dead wrong: the Supreme Court did not ignore the method of allotment in *Yakima Nation*; instead it expressly pointed out that the factual

question whether the land was allotted pursuant to the General Allotment Act, or some other statute, and the legal question of whether it makes any difference, was left for resolution on remand of the case. Further, the Supreme Court, in *Yakima Nation*, specifically grounded its decision upon section 5 of the General Allotment Act as amended by the Burke Act. It did not make a blanket holding that any removal of restrictions against alienation of Indian trust land, no matter under what statute or treaty, automatically subjected the land to state taxation.

But the Ninth Circuit didn't stop with merely equating alienability with taxability; it went on to hold that 25 U.S.C. § 177 did not provide inalienability to land purchased by the Lummi Tribe in fee simple status, citing *South Carolina v. Catawba Indian Tribe*, 476 U.S. 498 (1986). The lone dissenting judge in *Lummi Indian Tribe* pointed out that the flawed analysis of the majority missed the central point in *Yakima Nation*: namely, that the Supreme Court based its opinion specifically on a finding that the General Allotment Act showed an unmistakably clear congressional intention to subject the land to state taxation.

When *Lummi Indian Tribe* reached the Supreme Court, it denied review and left the Ninth Circuit's flawed reasoning standing for now. Nevertheless, the dissenting judge has correctly analyzed the law, especially in light of the per se rule of *Cabazon*, and it would seem that upon presentation of a proper case, the Supreme Court should reverse the holdings of *Lummi Indian Tribe.*

Note that had the litigating tribes been organized under the Indian Reorganization Act, they could have invoked section 16 of the IRA to prevent any state foreclosure on tribally owned lands. Section 16 provides, in pertinent part, that:

In addition to all powers vested in any Indian tribe or tribal council by existing law, the constitution adopted by said tribe shall also vest in such tribe or its tribal council the following rights and powers: . . . *to prevent the sale, disposition, lease, or encumbrance of tribal lands, interest in lands, or other tribal assets without consent of the tribe* . . . .

25 U.S.C. § 476.

In *Matter of City of Nome, Alaska*, 780 P.2d 363 (Alaska 1989), the Alaska Supreme Court considered an attempt by the City of Nome to foreclose on fee-owned land owned by the Nome Eskimo Community, an IRA tribe. The court examined the history of the IRA and found that section 16 was designed with the broad purpose of preventing the loss of tribal lands and assets, and that since the Nome Eskimo Community had not consented to a tax lien, or a tax foreclosure and sale of its non-reservation fee land, it could not be foreclosed upon.

(3) *Southern Ute Indian Tribe v. The Board of County Commissioners of the County of La Plata*, 855 F. Supp. 1194 (D. Colo., 1994). At least one federal district court agrees with the reasoning above and has properly interpreted *Yakima Nation* as hinging upon an express congressional intent to subject Indian lands to state taxation. *Southern Ute Indian Tribe v. The Board of County Commissioners of the County of La Plata* dealt with attempts to impose state taxes upon tribal fee lands inside the Southern Ute Reservation bought either from Indian allottees or homesteaders. The district court carefully analyzed *Yakima Nation* and *Lummi* and

concluded that the Supreme Court has not made alienability the sole prerequisite to taxability. The Court specifically agreed with the dissenting judge's analysis in *Lummi* and held that:

I think Judge Beezer is right. Alienability in *Yakima* and *Goudy* was important only as an indicator of congressional intent to permit taxation in that the Court thought it illogical the Congress would have intended to permit conveyance of land yet hold it immune from taxation. See Yakima, 112 S. Ct. at 691; Goudy, 203 U.S at 149. It was not an independent justification for alienability. Furthermore, if alienability were the only test, the court would not have left open the question in *Yakima* whether patenting under an act other than the General Allotment Act would require a different result.

1994 WL at 267913, Slip Op. at *12.

The Court then turned to the 1880 and 1895 Acts, under which the Southern Ute Reservation was allotted, to search for congressional intent to subject the land, once out of trust, to state taxation. The specific language of the statutes provided for taxability only upon the ending of the trust period and a presidential order lifting the restriction against alienability. But neither occurred before enactment of the Indian Reorganization Act of 1934, which specifically extended all trust periods and all restrictions against alienability until further direction by Congress.

On this basis, the district court concluded that, with respect to tribal fee lands originally allotted to an Indian, while Congress had authorized the trust period to end upon such lands, neither Congress nor the President had ever lifted the ban on taxability, and thus, the 1880 and 1895 Acts still applied to preclude Colorado state taxes. With respect to tribal fee lands originally homesteaded by non-Indians, the Court concluded that in the absence of any showing of congressional intent to subject those lands to state taxes, they also could not be taxed by Colorado.

On appeal, the Tenth Circuit Court of Appeals held the case unripe for adjudication because the County had merely threatened to impose taxes (except as to one parcel where the issue had become moot). *Southern Ute Indian Tribe v. La Plata County*, (unreported), 1995 WL 427683 (10th Cir. 1995). Judge Henry dissented, noting that the district court addressed issues of ripeness and correctly reached issues for the sake of efficiency.

It thus appears that further clarification of the Ninth Circuit's analysis in *Lummi Indian Tribe* will have to come from other cases. At least two federal district courts have followed *Lummi Indian Tribe* and the Sixth Circuit Court of Appeals is likely to address the matter soon in *United States and Saginaw Chippewa Indian Tribe of Michigan v. Michigan*, Nos. 95-1574 and 95-1575.

II. FEDERAL INCOME TAXATION AND INDIAN TRIBES.

A. INDIAN TRIBES ARE NOT TAXABLE.

1. The Internal Revenue Code. The Internal Revenue Code nowhere imposes income taxes on Indian tribes. Congress did not intend to limit the ability of tribes to carry out their sovereign

duties by imposing federal income tax on tribal income. This statement makes an important distinction. Some entities are not subject to federal taxes because they are *exempted* from taxes by certain provisions of the Internal Revenue Code. That is, they are otherwise taxable entities, but the Internal Revenue Code itself excuses them from taxation. Indian tribes, on the other hand, are not taxable entities in the first place, with respect to income tax. The applicability of other federal taxes to tribes and tribal entities is outside the scope of this outline.

2. Revenue Rulings. The IRS itself has recognized that Indian tribes are not within the income coverage of the Internal Revenue Code. In Revenue Ruling 67-284, it said "Income tax statutes do not tax Indian tribes. The tribe is not a taxable entity." Rev. Rul. 67-284, 1967-2 C.B. 55, *modified on another issue* by Rev. Rul. 74-13, 1974-1 C.B. 14.

In Revenue Ruling 81-295, 1981-2 C.B. 15, the IRS supplemented Revenue Ruling 67-284. The ruling concerned an Indian tribal corporation organized under Section 17 of the Indian Reorganization Act of 1934 ("IRA"), 25 U.S.C. § 477. Under section 16 of the IRA, Indian tribes were authorized to organize for governmental purposes with a constitution and by-laws. Under section 17 of the IRA, they were authorized to form federally-chartered tribal corporations for business purposes. In the case dealt with in the ruling, the tribe had organized under both sections 16 and 17 of the IRA. It had a constitution and by-laws and a separate corporate charter which organized a federal membership corporation consisting of the present and future members of the tribe. *The purpose of the corporation was to conduct communal economic effort to support the tribe's members and to enable the tribe to be self-sufficient*. The ruling holds that the corporation shares the tribe's immunity from federal income tax. The ruling quotes a line from the Supreme Court's decision in *Mescalero Apache Tribe v. Jones*, 411 U.S. 145 (1973), as follows:

The question of tax immunity cannot be made to turn on the particular form in which the tribe chooses to conduct its business.

411 U.S. at 157 n.13.

In Revenue Ruling 94-12, 1994-12 I.R.B., however, the IRS *did* use the particular form in which a tribe chooses to conduct business as the determining factor. In that ruling, the IRS confirmed that the business income of Indian tribes doing business under either section 16 or 17 of the IRA, whether earned on or off the reservation, would be exempt. It ruled, however, that income of a tribally-owned state corporation would *not* be exempt. The Ruling is further discussed below.

Note that an IRS General Counsel Memorandum issued in 1982, Gen. Couns. Mem. 38,853 (May 17, 1982), questioned whether off-reservation income of tribes should be taxed, citing the Supreme Court's decision in *Mescalero Apache Tribe v. Jones* (1973). However, Revenue Ruling 94-12 indicates that the IRS has abandoned this approach in favor of an approach that analyzes the form in which the tribe chooses to do business. Thus, the business income of a tribe, including income of an unincorporated commercial business and income of a corporation under section 17 of the IRA, is exempt whether earned on or off reservation.

3. Basis for the Exemption of Tribal Income. The rationale behind Revenue Ruling 67-284 is that Congress never intended to impose income tax on tribal income. Tribes, as sovereign governments, should not be restricted or guided by the income tax laws when they perform sovereign functions. Also, tribes should not be forced to pay income tax in order to provide general revenue funds for the federal government when the tribe would otherwise use the same money to provide local governmental services. In addition, imposition of income tax is inconsistent with federal trust responsibilities and the federal policy of encouraging tribal independence and self-determination. Given these policy considerations, the absence of any code provision expressly imposing income tax on tribes simply reinforces the IRS conclusion concerning the intent of Congress.

The position of the IRS in Revenue Ruling 67-284 that tribes are not taxable is very similar to its position, first announced in 1935, that states are not taxable. In General Counsel Memorandum 14,407 (1935), the IRS considered the taxability of income earned by a state in running liquor stores. The sole Code provision exempting state income covered only income derived in the course of exercising any "essential governmental function." (That provision survives today in section 115 of the Code.) The Supreme Court had previously ruled that liquor distribution did not qualify as an essential governmental function, and that there is no impediment under the United States Constitution to federal taxation of state liquor stores. *South Carolina v. United States*, 199 U.S. 437 (1905). Thus, if the language quoted provided the only exemption from taxation, state liquor store income would be taxed under the Code.

In rejecting this approach, the IRS noted that nothing in the Code expressly provided for taxation of state income. The Code only purports to tax "individuals" and "corporations." The IRS decided that the express exception for state income quoted above applied only to state instrumentalities which are separate from the state itself, and which might otherwise qualify as "corporations" subject to tax under the Code. Congress, the Service decided, never meant to restrict the sovereign powers of the state by making it subject to income tax:

It is suggested that Congress, in not taxing the income of States, may well have been motivated by a desire not to limit the activities in which States might otherwise engage. The line between those revenue-producing activities of a State which are "governmental" and those which are "proprietary" is one which is in its nature difficult to draw and which has as yet been only faintly traced by decisions of the courts. For example, while the conduct or operation of prisons is strictly within the sovereign functions of the State, the revenue derived from the manufacture and sale of prison-made merchandise may or may not be the essential result of a governmental activity. Similarly, such activities as the loaning of State funds or the sale of surplus properties are of a character which makes it difficult to predict in which category they would be placed. It may be assumed that Congress did not desire in any way to restrict a State's participation in enterprises which might be useful in carrying out those projects desirable from the standpoint of the State Government which, on a broad consideration of the question, may be the function of the sovereign to conduct; and it may reasonably be considered that it was the possibility of such restriction which persuaded Congress not to include State income within the subjects taxed by the various Revenue Acts since 1913.

Rev. Rul. 67-284, 1967-2 C.B. 55. The IRS still follows this reasoning in holding that a state's income is exempt from federal taxation. *See e.g.,* Rev. Rul. 77-261, 1977-2 C.B. 45; and Priv. Ltr. Rul. 84-53-038 (1984).

4. Taxation of Tribally-Owned Corporations. As noted above, Revenue Ruling 94-12 holds that income earned from commercial business by a corporation (and perhaps any other legal entity recognized under state law) organized by a tribe under state law is subject to federal income tax, whether earned *on or off* the tribe's reservation. This ruling confirms two private letter rulings issued in 1987, Priv. Ltr. Rul. 88-02-017 (October 9, 1987) and Priv. Ltr. Rul. 88-03-013 (October 19, 1987). The corporations involved in these letter rulings were both state-chartered corporations. The rulings concluded that tribally-owned corporations were subject to federal income tax for off-reservation activities.

5. Additional Questions. While Revenue Ruling 94-12 clarifies the IRS position somewhat, at least two additional issues are unclear.

a. "Non-commercial Business" Income. Revenue Ruling 94-12 discusses specifically "income earned in the conduct of commercial business." Whether or not this was meant to include other kinds of income, such as investment income, is not clear. However, there appears to be no reason why all income of a tribal entity, which otherwise qualifies under the IRS test, shouldn't be exempt.

b. Other Tribal Entities. Revenue Ruling 94-12 deals specifically only with unincorporated businesses and entities under section 17 of the IRA. Presumably, however, tribes which rejected the IRA, but which are federally-recognized, would still qualify as tax-exempt entities, as would traditional and IRA Alaskan tribal and village (non-ANCSA) organizations.

6. Off-Reservation Treaty Fishing Income. A specific exemption for treaty fishing income is provided in Subtitle E, Title III of TAMRA, Pub. L. 100-647. Section 3041 of the Act provides that income to a "qualified Indian entity" is exempt if it meets the other tests of the statute. I.R.C. § 7873(a)(1)(B). A qualified Indian entity includes any entity in which all of the equity interests in the entity are owned by an Indian tribe or its members or spouses. *Id.* § 3041(A). In case of income from the processing or transporting of fish, there are additional tests which must be met. I.R.C. § 7873(b)(3).

B. TAX BENEFITS RELATED TO FEDERAL INCOME TAXES.

While Indian tribes enjoy a broader *immunity* from federal taxes than states, it was not until enactment of the Tribal Governmental Tax Status Act of 1982 that the Internal Revenue Code extended to Indian tribes the indirect tax *benefits* which have traditionally been extended to states and their subdivisions.

1. Charitable Contributions.

a. Income Tax Deduction. A charitable contribution made directly to an Indian tribe or a governmental subdivision of an Indian tribe which exercises one or more substantial

governmental functions of the tribe itself is deductible by the taxpayer for federal income tax purposes under the Tax Status Act. 26 U.S.C. § 7871(a)(1)(A).

b. Estate Tax Deduction. A charitable contribution made directly to an Indian tribe, or a governmental subdivision of an Indian tribe which exercises one or more substantial governmental functions of the tribe itself, is deductible by an estate for federal estate tax purposes under the Tax Status Act. 26 U.S.C. § 7871(a)(1)(B).

c. Gift Tax Deduction. A charitable contribution made directly to an Indian tribe, or a governmental subdivision of an Indian tribe which exercises one or more substantial governmental functions of the tribe itself, is deductible by a taxpayer for federal gift tax purposes under the Tax Status Act. 26 U.S.C. § 7871(a)(1)(C).

2. Interest on Governmental Obligations. A different kind of benefit is conferred on state and local governments, and now upon Indian tribes, by section 103 of the Internal Revenue Code. Section 103 provides that gross income does not include interest on "the obligations of a state, a territory or a possession of the United States, or any political subdivision of any of the foregoing, or of the District of Columbia." This section enables states and municipal corporations to issue various kinds of bonds to finance their activities. These bonds are highly marketable because their owners do not have to pay income tax upon interest earned from the bonds. The Tax Status Act added Indian tribal governments, and political subdivisions of Indian tribal governments which have been delegated the right to exercise one or more of the substantial governmental functions of the Indian tribal government, to the list of governmental entities entitled to issue tax exempt bonds. In 1987 Congress amended the Tax Status Act to restrict tribal tax-exempt bonds to those issued in connection with transactions which are customarily undertaken by state and local governments with general taxing powers.

3. Indian Employment Credit. Pub. L. 103-66 added section 45A to the Internal Revenue Code, providing a tax credit for increases in reservation employment since 1993. Qualified employees, for the purpose of the tax credit, are enrolled tribal members of a federally recognized Indian tribe, or spouses of enrolled members, who live on or near a reservation and work mainly on the reservation and who receive no more than $30,000 in annual wages (a figure that will be adjusted upward to account for inflation after 1994). The 20% tax credit for increased employment of tribal members and spouses is subject to certain restrictions. For example, at least half of the employees' wages must be for services performed in a trade or business, § 45A(c)(4), and employees involved in gaming or working in a building housing a gaming activity, are not included. I.R.C. § 45A(c)(5). Nevertheless, this section could provide a substantial tax advantage for non-tribally owned businesses employing tribal members on reservations.

4. Accellerated Depreciation for Property on Reservations. Pub. L. 103-66 also added a new subsection to I.R.C. § 168 providing for shorter depreciation periods for property used to conduct a trade or business within an Indian reservation. Again, property used to conduct or house gaming operations is not included, nor is property regularly used outside the reservation. Nevertheless, "qualified Indian reservation property" may be depreciated more quickly than property in a similar class used elsewhere; for example, three-year property may be depreciated

in two years, "seven-year property" may be depreciated in four years, etc. As an example, rental of real estate within an Indian reservation is the kind of business that may qualify for accellerated cost recovery under I.R.C. § 168(j).

5. State and Local Income Taxes. The Internal Revenue Code (§164) allows a deduction for various taxes paid to state and local governments. These include: (a) real property taxes, (b) personal property taxes, (c) state, foreign and local income, war profits, and excess profit taxes, and (d) the environmental tax imposed by I.R.C. § 59A, and the GST (i.e., generation skipping transfer tax) on income distributions. *See* I.R.C. § 164(a). The Code also allows a business expense deduction for various state and local taxes which are paid in carrying on a trade or a business. Such taxes paid to Indian tribes are now tax deductible by virtue of the Tax Status Act. 26 U.S.C. § 7871(a)(3).

Because of the amendments to I.R.C. § 164, general sales taxes are no longer deductible. Since I.R.C. § 7871(a)(3) is keyed into I.R.C. § 164 for the deductibility of these types of taxes, sales taxes paid to tribes will no longer be tax deductible under the Indian Governmental Tax Status Act of 1982.

III. TRIBAL TAXES.

A. INTRODUCTION: THE NEED AND THE POWER TO TAX.

1. The Need for Taxation. Indian tribes, like other governments, depend upon revenue to finance their operations. To a unique extent Indian tribes have historically obtained revenue from sources other than taxes. Nonetheless, given the overwhelming national thrust to reduce the federal deficit, many tribes today recognize that the strength of their governments can no longer be left to depend upon federal government support and that their budget needs are outstripping the returns from tribal resource development and economic enterprises. Thus, some tribes have already begun to levy taxes on activities within their jurisdictions, and other tribes are giving serious attention to the development of tribal tax programs as a means of governmental support.

A tax can be thought of as any governmental regulation which increases the cost of carrying on an activity, engaging in a transaction, or owning property. Thus, a variety of tribal laws might be regarded as tax laws even though they do not require the payment of revenue to the tribe. For example, tribal land use and building code ordinances which prescribes zoning and construction requirements, and environmental safeguards for developments on lands situated within the reservation, do not require anyone to pay a tax to the tribe, but probably will result in increased costs incurred in order to comply. While this section is concerned only with taxation in the ordinary sense of levying and collecting revenues, it is helpful to think of taxation in the broader sense, because to some degree all exercises of tribal regulatory powers are governed by the same legal principles. The rules that govern a tribe's power to regulate hunting and fishing, land use, and air quality on its reservation will also have some application to its taxing measures.

The Supreme Court and lower federal courts have been active in defining the limits of tribal powers, as this has been one of the major issues raised by Indian tribes and their opponents in the ongoing legal battle to preserve the fabric of tribal life in a world which constantly threatens it. It

is important to understand the limits which the Supreme Court has placed on tribal jurisdiction within Indian reservations while at the same time exercising that jurisdiction to the fullest extent possible. The issues of greatest concern currently are tribal powers over non-Indians, generally, and over non-Indians on non-Indian land, in particular.

A good example of the broad exercise of tribal jurisdiction was considered by the Ninth Circuit Court of Appeals in *Queets Band of Indians v. Washington*, 765 F.2d 1399 (9th Cir. 1985), which involved an ordinance of the Quinault Tribe providing for tribal licensing of tribally-owned vehicles only. The court conducted the "particularized inquiry" and weighed tribal interests against state interests. The court concluded that the Tribe's exercise of inherent sovereignty in licensing and registering its vehicles carries with it sufficient "preemptive" force to require that the State of Washington afford reciprocal recognition of tribal licenses and not require state licenses when tribal vehicles are used outside the reservation. The same principle was adopted by the Minnesota Supreme Court in *Red Lake Band of Chippewa Indians v. Minnesota*, 248 N.W.2d 722 (Minn. 1976), in a case which involved tribal licensing not only of tribally-owned vehicles, but of all vehicles owned by tribal members.

The implication of these cases is that a tribe has inherent legal authority to license both tribal vehicles and vehicles of tribal members with preemptive effect. That is, the tribe's licensing statute can squeeze out the state statute, and thus, prevent the need for double licensing. Of course, the tribe's regulatory ordinance carries with it the right to tax the licensing of vehicles.

2. The Sources of Tribal Taxing Power. The sources of an Indian tribe's power to levy taxes are two: its sovereign governmental authority to regulate its own territory and, with respect to non-members, its power to exclude them from the reservation. A clear statement by the Supreme Court of these twin sources of tribal taxing powers came in *Washington v. Confederated Tribes of the Colville Reservation*, 447 U.S. 134 (1980).

Indian tribes have long been recognized as having taxing powers. This power is regarded as one of the aspects of tribal sovereignty. The famous 1934 Opinion of Solicitor Margold, which was quoted in *Washington v. Confederated Tribes*, states this principle as follows:

Chief among the powers of sovereignty recognized as pertaining to an Indian tribe is the power of taxation. Except where Congress has provided otherwise, this power may be exercised over members of the tribe *and* over *nonmembers*, so far as such non-members may accept privileges of trade, residence, etc., to which taxes may be attached as conditions.

Opinion of the Solicitor of the Department of Interior, 55 I.D. 14, 46 (1934) (emphasis added).

The power to tax is a fundamental attribute of sovereignty which Indian tribes have retained. That is, the federal government has never taken from them and they have never yielded this original part of their overall governmental power. In *Iron Crow v. Oglala Sioux Tribe*, 231 F.2d 89 (8th Cir. 1956), a member of the Oglala Sioux Tribe, who owned trust land within the Pine Ridge Reservation, leased the land to a non-member of the tribe. The tribe levied a tax on the nonmember for the privilege of raising stock on the land, and the Indian owner challenged the tax. The Eighth Circuit Court of Appeals upheld the tax, and in the process said:

Inasmuch as it has never been taken from it, the defendant Oglala Sioux Tribe possesses the power of taxation which is an inherent incident of its sovereignty. The Tribe has seen fit to give orderly implementation to that power through the adoption of a constitution which, among other things, has specifically provided for the levy of taxes. Such action was taken in accordance with the provisions of the Indian Reorganization Act . . . .

We conclude from the original precept of tribal sovereignty and the fact that the power of the Oglala Sioux Tribe to impose the tax or license in question has not been pretermitted by any federal statute or agency ruling thereunder, but, to the contrary, has been implemented by the Indian Reorganization Act . . . that such power still exists.

231 F.2d at 99.

In its clearest statement regarding tribal taxing powers, the Supreme Court in *Confederated Tribes* said:

The power to tax transactions [with non-Indians] occurring on trust lands and significantly involving a tribe or its members is a fundamental attribute of sovereignty which the tribes retain unless divested of it by federal law or necessary implication of their dependent status.

The widely held understanding within the Federal Government has always been that federal law to date has not worked a divestiture of Indian taxing power. Executive Branch officials have consistently recognized that Indian tribes possess a broad measure of *civil jurisdiction* over the activities of non-Indians on Indian reservation lands in which the tribes have a significant interest.

447 U.S. at 152 (emphasis added).

Confederated Tribes became the foundation of the Supreme Court's opinion in the very important case of *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130 (1982). Citing the above language, the Supreme Court in *Merrion* continued:

The power to tax is an essential attribute of Indian sovereignty because it is a necessary instrument of self-government and territorial management. This power enables a tribal government to raise revenues for its essential services.

455 U.S. at 137.

The Court in *Merrion* refused to accept the argument that a tribe's taxing power is only *negatively* derived, that is, comes from its power to exclude nonmembers, and instead held that it is *positively* derived from broad principles of tribal sovereignty:

The power does not derive solely from the Indian tribe's power to exclude non-Indians from tribal lands. Instead, it derives from the tribe's general authority, as sovereign, to control economic activity within its jurisdiction, and to defray the cost of providing governmental services by requiring contributions from persons or enterprises engaged in economic activities within that jurisdiction.

455 U.S. at 137.

Merrion concerned a tribal severance tax on oil and gas production which the Jicarilla Apache Tribe levied on non-Indian oil and gas companies who extracted oil and gas from tribal lands on the reservation. The oil and gas companies had long-term leases with the Tribe which gave them the right to go on tribal land, drill for, and extract oil and gas. The companies argued that when the Tribe entered into those leases it gave up the power to exclude the companies from the reservation since those leases themselves were permission from the Tribe to be on the reservation. The companies argued that since the Tribe's power to tax non-Indians came solely from its power to exclude them from the reservation, the Tribe could not tax the non-Indian companies which it had, by lease, agreed not to exclude. The Supreme Court made it clear that Indian tribes have *governmental power over non-Indians, not simply the authority that a private landowner has over persons who enter his land*:

Thus, the views of the three federal branches of government, as well as general principles of taxation, confirm that Indian tribes enjoy authority to finance their governmental services through taxation of non-Indians who benefit from those services. Indeed, the conception of Indian sovereignty that this Court has consistently reaffirmed permits no other conclusion. As we observed in *United States v. Mazurie*, 419 U.S. 544, 557 (1975):
"Indian tribes within `Indian country' are a good deal more than `private, voluntary organizations.' They `are unique aggregations possessing attributes of sovereignty over both their members and their territory' . . . ."

Adhering to this understanding, we conclude that the Tribe's authority to tax non-Indians who conduct business on the Reservation does not simply derive from the Tribe's power to exclude such persons but is an inherent power necessary to tribal self-government and territorial management.

455 U.S. at 140.

Thus, it is true beyond doubt that Indian tribes have the power to tax Indians and *under certain circumstances* non-Indians.

3. Limitations on the Power to Tax. However, challenges to exercises of tribal regulatory powers, especially regulatory powers over non-Indians, have been made and, in some cases, upheld on the grounds that tribal jurisdiction is more limited than that of other governments. These limitations have been "found" in decisions of the Supreme Court. The overall purpose of this section on tribal taxes is to identify the conditions under which tribal taxing powers exist and to explore the possible limitations on these powers in order to provide guidelines for the development of tribal tax programs. In this context, the term "tax program" is used rather than a term such as "tax ordinance" or "tax law" in order to convey the idea that a tribe's power to tax activities, transactions, and property will depend upon a number of factors and not simply the written tax laws themselves. Tribal tax legislation, no matter how skillfully written, cannot support tribal taxing measures without a well-laid plan which involves actual tribal operations and takes into consideration existing social and political conditions.

Apart from its *power* to tax, a tribe should also examine the wisdom of doing so, as well as the ability of the tax *base* to support the tax, and the tribe's ultimate ability to *enforce* its tax laws against unwilling taxpayers.

B. EXERCISING THE POWER TO TAX.

1. Taxation of Indians. Tribes clearly have broad power to tax their own members. This power extends to activities on both "Indian" and "non-Indian" land within the tribe's reservation. It also extends to off-reservation and nonreservation activities when the tribe can show a significant interest in the activity. For example, tribes should be able to tax their members on the basis of the rights or privileges which attach to tribal citizenship, such as the exercise of off-reservation treaty hunting and fishing rights. *Cf. Settler v. Lameer*, 507 F.2d 231 (9th Cir. 1974) (off-reservation regulation).

As we have already seen, Indians who are not members of the tribe stand in a different category. In *Confederated Tribes*, the Supreme Court made a distinction between member and nonmember reservation Indians. It said that, although Washington could not impose a sales tax on members of the Colville Tribe who purchased cigarettes on the reservation, the state could collect the tax from Indians on the reservation who were not Colville members. In other words, a state has *greater* power over a nonmember Indian on a reservation than it has over a member of the tribe of that reservation. Prior to 1990, a question existed as to whether the Supreme Court would hold, by the same token, that an Indian tribe has *less*power over nonmember Indians on its reservation than it has over its own members.

In view of a recent evolution of the law in the criminal context, that question may have been answered negatively by the Supreme Court. In *Duro v. Reina*, 495 U.S. 676, 109 L. Ed.2d 693 (1990) the Supreme Court had held that a tribal court has no power to try nonmember Indians for violations of tribal criminal laws. However, the Court carefully based its ruling, in part, upon the markedly different development of principles governing civil jurisdiction in Indian country from those governing criminal jurisdiction. The Court pointed out that retained civil jurisdiction by Indian tribes typically involves situations involving property ownership, or consensual relationships between nonmembers and the tribe or its members, whereas criminal jurisdiction involves a far more direct intrusion on personal liberties. This distinction, together with other legal considerations not relevant here, led the Supreme Court to hold that Indian tribes have been divested of their criminal jurisdiction over nonmember Indians and may no longer exercise it unless it is restored by Congress.

As a result of the decision, Congress did, indeed, in 1990 restore criminal jurisdiction over nonmember Indians to tribes by amending the term "powers of self-government" in the Indian Civil Rights Act, PL 101-511, 25 U.S.C §§ 1301-2, to clarify that it includes inherent criminal jurisdiction over all Indians, and by simultaneously defining the term "Indian" to include all Indians, regardless of membership.

Because civil jurisdiction involves a much more insignificant intrusion on personal rights, and because Congress saw fit to restore to tribes their criminal jurisdiction over nonmember

Indians, the Supreme Court will now be less likely to hold that the jurisdiction of tribes over nonmember Indians is less than that exercised over their own members.

2. Taxation of Non-Indians.

a. *Washington v. Confederated Tribes of the Colville Reservation*, 447 U.S. 134 (1980). Non-Indians are the principal reason why tribal tax programs must be well-founded, thoroughly planned and precisely defined. The Supreme Court has avoided telling Indian tribes that all non-Indians within their reservations are within their taxing powers. In fact, it has quite clearly said that in some circumstances non-Indians are not subject to tribal regulations. The Court's statement in *Confederated Tribes*, quoted above, shows how it feels about this issue. Let us reexamine that language, and this time notice the *limitations* the Court places on tribal taxing authority:

The power to tax transactions [with non-Indians] occurring on trust lands and significantly involving a tribe or its members is a fundamental attribute of sovereignty which the tribes retain unless divested of it by federal law or necessary implication of their dependent status.

447 U.S. at 152.

This statement is somewhat misleading. While it might appear to limit tribal taxing power to transactions occurring on trust land, the power is definitely not so limited. The Court was simply restricting its decision to the facts of the case, which involved cigarette sales on trust lands. The holding cannot be read to mean that a tribe may never tax a transaction which occurs on nontrust land.

b. *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130 (1982)**.** The Supreme Court's decision in *Merrion v. Jicarilla Apache Tribe* makes it clear, although in a roundabout way, that tribal taxing jurisdiction does indeed extend in certain circumstances to non-Indian-owned reservation land. In the opinion in *Merrion*, the Court had occasion to discuss the early decision of the Eighth Circuit Court of Appeals in *Buster v. Wright*, 135 F. 947 (8th Cir. 1905), regarding whether a tribe's authority to tax non-Indians comes exclusively from its power to exclude them from the reservation. The dissent in *Merrion* cited *Buster v. Wright* in support of this argument. However, Chief Justice Marshall, writing for the majority of the Court, pointed out that *Buster v. Wright* actually stands for the opposite proposition; that is, that the taxing power does not derive solely from the power to exclude, but is rather a general governmental power. The Court said:

This result was explicitly rejected in *Buster v. Wright*. In *Buster*, deeds to individual lots in Indian territory had been granted to non-Indian residents, and cities and towns had been incorporated. As a result, Congress had expressly prohibited the Tribe from removing these non-Indian residents. Even though the ownership of land and the creation of local governments by non-Indians established their legitimate presence on Indian land, the Court held that the Tribe retained its power to tax. The Court concluded that [n]either the United States, nor a state, nor any other sovereignty loses the power to govern the people within its borders by the existence of towns and cities therein endowed with the usual powers of municipalities, *nor by the ownership nor occupancy of the land within its territorial jurisdictions by citizens or foreigners* . . . . This

result confirms that the Tribe's authority to tax derives not from its power to exclude, but from its power to govern and to raise revenues to pay for costs of government.

455 U.S. at 143 (emphasis added). In this manner *Merrion* makes it clear that a tribe's jurisdiction may embrace non-Indian-owned lands within its reservation.

c. *Montana v. United States*, 450 U.S. 544 (1981)**.** The second element of the holding in *Confederated Tribes*, i.e., "significantly involving a tribe and its members," reflects a true limitation on tribal taxing power. It is certain that the Supreme Court will require a tribe to demonstrate a *significant interest* in the non-Indian transactions and activities it taxes, particularly if they occur on nontrust land. In *Montana v. United States*, the Court held that a tribe did not have a significant interest in certain non-Indian activities merely because they occurred within the exterior boundaries of the reservation. Something more is needed. *Montana v. United States* involved the ownership of the bed and banks of the Little Big Horn River on the Crow Indian Reservation in Montana, and the Crow Tribe's power to regulate (actually, prohibit) non-Indian hunting and fishing on nontrust land within the reservation. The decision, which held that the State of Montana, rather than the Crow Tribe, held title to the bed and banks of the river and that the Tribe lacked the power to regulate non-Indian hunting and fishing on non-Indian fee land within the Reservation, showed that the Supreme Court may be disposed toward limiting tribal powers. In the opinion, the Court made the disturbing comment that, as a general proposition, "the inherent sovereign powers of an Indian tribe do not extend to the activities of non-members of the tribe." It then retreated from this position, saying:

To be sure, Indian tribes retain inherent sovereign power to exercise some forms of civil jurisdiction over non-Indians on their Reservations, even on non-Indian fee lands. A tribe may regulate, through *taxation*, licensing, or other means, the activities of non-members who enter consensual relationships with the tribe or its members, through commercial dealing, contracts, leases, or other arrangements. A tribe may also retain inherent power to exercise civil authority over the conduct of non-Indians on *fee* lands within its Reservation when that conduct threatens or has some direct effect on the political integrity, the economic security, or the health or welfare of the tribe.

450 U.S. at 565 (citations omitted) (emphasis added).

In 1982 the Supreme Court, in *Merrion*, discussed the power of tribes to tax non-Indians in different, more expansive terms than the above language from *Montana v. United States*. It said:

Viewing the taxing power of Indian tribes as an essential instrument of self-government and territorial management has been a shared assumption of all three branches of the Federal Government . . . . In *Colville* the Court relied in part on a 1934 opinion of the Solicitor for the Department of the Interior. In this opinion, the Solicitor recognized that, in the absence of Congressional action to the contrary, the tribes' sovereign power to tax "may be exercised over members of the tribe and over non-members, so far as such non-members may accept privileges of trade, residence, etc., to which taxes may be attached as conditions." . . . *Colville* further noted that official executive pronouncements have repeatedly recognized that "Indian tribes possess a broad measure of civil jurisdiction over the activities of non-Indians on Indian Reservation lands in which the tribes have a significant interest" . . . , including jurisdiction to tax.

455 U.S. at 139.

The term "consensual", used in *Montana v. United States*, may have sounded a bit like "contractual." *Merrion*, however, makes it clear that the term has to do with benefits or privileges which a non-Indian may enjoy and which derived from a tribe's territorial control of its reservation. For example, it may mean simply "consent" to participate in business in the civilized environment on the reservation. Referring to the non-Indian oil and gas companies who had leases on tribal lands, the Court in *Merrion* said:

The petitioners avail themselves of the "substantial privilege of carrying on business" on the Reservation . . . . They benefit from the provision of police protection and other governmental services, as well as from "the advantages of a civilized society" that are assured by the existence of tribal government . . . . Numerous other governmental entities levy a general revenue tax similar to that imposed by the Jicarilla Tribe when they provide comparable services. Under these circumstances, there is nothing exceptional in requiring petitioners to contribute through taxes to the general cost of tribal government.

Id. at 137-38.

d. *Burlington Northern Railroad v. Blackfeet Tribe*, 924 F.2d 899 (9th Cir. 1991), *cert. denied* 112 S. Ct. 3013 (1992)**.** If tribes have broad taxing powers over tribal trust land and more limited taxing powers over non-Indian fee land, what kind of taxing powers do tribes have over land held under a federally-granted right-of-way? The Ninth Circuit Court of Appeals considered this question in the *Burlington Northern* case involving a possessory interest tax by the Blackfeet Tribe on utility rights-of-way, and a property tax on utility property by the Fort Peck Tribe. In response to these taxes, Burlington Northern Railroad filed suit against the Tribes and tribal officers, seeking to enjoin the tax.

Burlington Northern argued that the congressional grant to the railroad of a right-of-way amounted to a grant of a fee-simple interest, leaving the Tribes with no interest in the underlying land. It argued that the tax was illegal for three reasons: (1) No consensual relationship existed between the Tribes and the railroad; (2) The Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act"), implicitly divested the Tribes of taxing authority of railroad right-of-ways; and (3) The tribal tax violates the Interstate Commerce Clause.

The Ninth Circuit rejected all of Burlington Northern's arguments and held that because nothing in the congressional grants of rights-of-way to Burlington Northern indicated a clear congressional intent to grant the railroad a fee title to the land rather than a simple right-of-way, Burlington Northern obtained only a right to cross the reservations. Borrowing a leaf from *Merrion*, the court found that Burlington Northern received the intangible benefits of a civilized society and the tangible benefits of police and fire protection and, therefore, was subject to the tribal taxes which were specifically enacted to defray the cost of providing governmental services. The Ninth Circuit easily disposed of the statutory and constitutional arguments by noting that the plain language of the 4-R Act referred to "states" or "subdivisions of states," and did not prohibit any Indian tribe from anything. Finally, the court held that commerce clause doctrine developed in the context of commerce between the states is not applicable to the Indian Commerce Clause. The Supreme Court denied review of the case.

e. *Brendale v. Yakima Indian Nation*, 492 U.S. 408 (1989)**.** This Supreme Court case, which dealt with tribal zoning authority over non-Indian fee land within the Yakima Reservation appears to foreshadow far-reaching effects on the exercise of tribal sovereign governmental powers within Indian reservations, and could affect the tribal tax power. The case involved a head on clash between the zoning laws of the Tribe and Yakima County. *Brendale* involved two separate cases which were decided together.

One case involved the "closed" area of the Reservation containing a total of 740,000 acres of land, of which 3%, or 25,000 acres, are held by Indians and non-Indians in fee. The remaining 97%, or 715,000 acres, are held in trust. The closed area has been closed to the general public since at least 1972, and the BIA has restricted the use of roads in the area to members of the Yakima Tribe and its permittees. The Yakima Nation zoning ordinance severely restricts permissible uses of land within the closed area. The other case involved the "open" area of the reservation, which is not restricted to the general public, and of which nearly 50% is held in fee either by Indians or non-Indians. The land within the open area is primarily used for grazing, agriculture, and residential and commercial development. Three incorporated towns lie within the open area. The population is primarily non-Indian. The tribal zoning ordinance establishes different restrictions within the open area than within the closed area. By its terms, the county zoning ordinance applies to all lands within the county, except the Indian trust land.

The combined judgment of the Supreme Court, which entered three separate opinions in these consolidated cases, is internally inconsistent because the Court was deeply divided over the issue of the nature and extent of tribal authority. In general, however, the case upheld tribal authority to zone non-Indian fee land inside the "closed" area, but denied tribal authority to zone non-Indian fee land in the "open" area. The case is not a tax case, but the Supreme Court's opinion regarding the open area modified the second test of tribal jurisdiction over a nonmember--at least in nontax cases. The Court first said that the Yakima Tribe had no power to exclude nonmembers from fee land inside the reservation; that power was taken away by the General Allotment Act. It then held that it would apply the Montana test, but warned that the second Montana test held only that a tribe "may" retain jurisdiction over nonmembers in certain circumstances. With that groundwork in place, the Court then modified the second Montana test as follows:

. . . Montana suggests that in the special circumstances of checkerboard ownership of lands within a reservation, the tribe has an interest under federal law, defined in terms of the impact of the challenged uses on the political integrity, economic security, or the health or welfare of the tribe. But, as we have indicated above, that interest does not entitle the tribe to complain or obtain relief against every use of fee land that has some adverse effect on the tribe. *The impact must be demonstrably serious and must imperil the political integrity, economic security or the health and welfare of the tribe. This standard will sufficiently protect Indian tribes while at the same time avoiding undue interference with state sovereignty and providing the certainty needed by property owners*.

106 L.Ed.2d at 363 (emphasis added). This much more difficult test can be expected to pose substantial difficulty for any tribal tax imposed on nonmembers for activities on fee land inside a reservation.

f. Rough Guidelines for Tribal Taxation. The full impact of the holdings in these cases will not be known until future cases raising these issues have been decided. However, the holdings leave Indian tribes with the following rough guidelines for the development of tribal tax programs which impose taxes on non-Indians:

(1) When a Tax on Non-Indians is Valid. A tribal tax on a non-Indian transaction or activity occurring within the bounds of the reservation will be upheld if: (a) The transaction or activity takes place on trust land; or (2) The transaction or activity takes place on non-Indian fee land and either: (i) The non-Indian is involved in a consensual relationship with the tribe or individual Indians; *or* (ii) The impact of the transaction or activity on the tribe is demonstrably serious and imperils the political integrity, economic security or the health and welfare of the tribe.

(2) When a Tax on Non-Indians is Invalid. A tribal tax on a non-Indian transaction or activity occurring within the bounds of the reservation will be struck down if: (a) The transaction or activity takes place on nontrust land and either: (i) The non-Indian is not involved in a consensual relationship with the tribe or individual Indians; *or* (ii) The impact of the transaction or activity on the tribe is not demonstrably serious and does not imperil the political integrity, economic security or the health and welfare of the tribe.

These criteria, of course, describe only the two possible extremes, and they leave several important questions unanswered. It is extremely important to note that neither *Montana* nor *Brendale* involved tribal tax power at all. The second *Montana* test provided a workable and rational basis for the application of tribal tax power to non-Indian fee lands, but its modification in *Brendale* leaves it virtually useless to a tribe and, indeed, a weapon which will undoubtedly be seized by those opposing tribal tax power. Their reliance upon it is misplaced, however, for the Supreme Court's prime reason for denying tribal zoning authority over non-Indian fee land in *Brendale* was loss of the tribe's power to exclude non-Indian fee land owners from open areas of the reservation; whereas, in *Merrion* the Court carefully pointed out that the tribal tax power is a free-standing, independent sovereign power which does not rest on the exclusion power. Nevertheless, these cases illustrate the point that tribal taxes will be judged on a case-by-case basis.

It is important that the first few of the cases challenging tribal taxes arise out of facts which strongly support tribal jurisdiction over nonmembers. What if the non-Indian activity simply takes place on trust land and does not involve a consensual relationship or imperil health, safety or welfare? Can a tribe tax the activity in that case? Clearly, the answer should be yes--that tribes have the right to tax non-Indians who enter into consensual relationships with Indians *or* who engage in activities on Indian land. As has been stressed above, the power to tax non-Indians present on Indian land within a reservation derives not only from the tribe's inherent sovereignty but also from the tribe's power to exclude nonmembers from that land. The United States Supreme Court in *Morris v. Hitchcock*, 194 U.S. 384 (1903), recognized the power to exclude and the related power of tribes to prescribe the terms and conditions upon which non-Indians may enter and do business on Indian land. The Court in *Merrion* recognized that one of the conditions that a tribe may attach to the right to enter is the requirement that the non-Indian pay taxes.

3. Providing Services to Non-Indians. One of the criteria mentioned above supporting tribal power to tax non-Indians deserves special attention. Today, when courts are questioning how much jurisdiction Indian tribes should have over non-Indians, it is important to answer with concrete justifications for asserting that jurisdiction. While the power of states to tax everyone within their jurisdictions goes largely unquestioned, Indian tribes will undoubtedly be forced to justify their taxing measures with facts which show that they have a substantive interest in the object of the tax. One way for a tribe to show that it has an interest in taxing non-Indians, even non-Indians living on fee land, is to provide them governmental services. Any tax imposed upon a non-Indian is more likely to be treated as fair and appropriate if the non-Indian taxpayer receives a return for his taxes in the form of services such as water, sewers, electricity, and fire and police protection.

The Supreme Court in *Confederated Tribes* suggested that a *state* tax imposed upon non-Indians on the reservation might infringe on the right of the tribal government to make its own laws and be ruled by them *if* the Tribe has a significant enough interest in the transaction or property being taxed. The Tribe's interest is measured as follows:

While the Tribes do have an interest in raising revenues for essential governmental programs, that interest is strongest when the revenues are derived from value generated on the Reservation by activities involving the Tribes and *when the taxpayer is the recipient of tribal services*.

447 U.S. at 156-57.

The tribal tax in *Confederated Tribes* was upheld, and in the above-quoted statement, the Supreme Court was referring to situations in which a tribal tax might preempt a state tax because the Tribe's interest in the taxing subject totally outweighs the state's interest. It was not speaking about the validity of a tribal tax on non-Indians in the first place. However, the statement does give a good indication of how a tribal tax might be judged in a lawsuit brought by a non-Indian challenging the tribe's right to tax him. If the non-Indian resides on trust land the tribe already has one basis for imposing its tax. Providing services, however, furnishes an additional basis for taxing. And if the non-Indian resides on fee land the tribe's public works, police or fire services provided to him could, in themselves, supply an adequate foundation for asserting governmental jurisdiction over him.

Merrion clearly suggests this result. As mentioned above, the Court there noted that the non-Indian oil and gas companies were receiving "benefits" of police protection and other governmental services, as well as the "advantages of a civilized society" that are assured by the existence of tribal government. What both *Confederated Tribes* and *Merrion* underscore is that a tribal tax must "attach" to some benefit or privilege which the non-Indian receives directly or indirectly from the tribe.

An example of a tribal tax on non-Indians withstanding a court challenge may be found in *Snow v. Quinault Indian Nation*, 709 F.2d 1319 (9th Cir. 1983), *cert. denied*, 467 U.S. 1214 (1984). There the United States District Court for the Western District of Washington upheld tribal license and business taxes imposed on non-Indians doing business on *non-Indian* land within the reservation. The court said that in *Confederated Tribes* the Supreme Court made it clear that the tax was permissible. The district court found that the Tribe provided fire, police,

social and welfare services, and recreational opportunities for Indians and non-Indians alike, regardless of the status of their land. The Ninth Circuit Court of Appeals affirmed the decision.

Other services which may be of equal importance are environmental services, such as air and water quality control. By establishing that it has a legitimate governmental interest in protecting the environment throughout its reservation, including fee lands, and by implementing such a plan, a tribe would broaden its basis for asserting jurisdiction, including taxing jurisdiction, over non-Indians.

4. The Preemptive Power of Tribal Taxes. A tribe and a state have *concurrent* taxing jurisdiction when they both have a right to tax a particular subject, regardless of the other's tax. Economically speaking, of course, there may not be room for both taxes, and the result of a tribal tax imposed on top of a state tax on a particular subject might be to tax that subject out of existence. This was the result of the Supreme Court's ruling in *Confederated Tribes*, 447 U.S. 134 (1980): Both the State of Washington and the Colville Confederated Tribes had the right to tax on-reservation sales of cigarettes to non-Indians. Since the tribal taxes combined with state taxes increased the price of on-reservation cigarettes above that of off-reservation cigarettes they would destroy the reservation cigarette market. Nonetheless, the Supreme Court held that the two taxes could *legally* coexist.

In other cases a state may have a right to impose a tax only so long as the tribe has not exercised its taxing power; that is, the tribe's power to tax, *when exercised*, becomes an exclusive power which preempts (displaces) the state tax. Both situations (concurrent jurisdiction and preemptive tribal jurisdiction) arise in cases involving non-Indians. The problem is to distinguish between those situations in which states and tribes have *concurrent* taxing jurisdiction and those in which a tribal tax will *preempt* a state tax.

As discussed earlier, the United States Supreme Court's decision in *Williams v. Lee*, 358 U.S. 217 (1959), forms the basis of the "tribal preemption" doctrine. In that case the Supreme Court considered the question whether a non-Indian licensed by the federal government as a federal trader could sue an Indian in state court on a debt arising out of business transacted on the reservation, and noted that it had been a basic federal policy to immunize Indians from state law since the early days of the nation. It summarized:

Essentially, absent governing Acts of Congress, the question has always been whether the state action infringed on the right of Reservation Indians to make their own laws and be ruled by them.

358 U.S. at 220. It held that the exercise of state jurisdiction in the dispute between the non-Indian and the Indian infringed upon tribal self-government and, therefore, was invalid.

Later, in *McClanahan v. Arizona State Tax Comm'n*, 411 U.S. 164 (1973), the Supreme Court clarified its holding in *Williams v. Lee*, saying that the self-government test was specifically designed to deal with situations where both a state and a tribe seek to apply their laws to an on-reservation transaction *involving both Indians and non-Indians*. It said:

It must be remembered that cases applying the *Williams* test have dealt principally with situations involving non-Indians. In these situations, both the tribe and the State could fairly claim an interest in asserting their respective jurisdictions. The *Williams* test was designed to resolve this conflict by providing that the State could protect its interest up to the point where tribal self-government would be affected.

411 U.S. at 179 (citations omitted).

Thus, when a state attempts to impose a tax on a reservation activity or transaction involving non-Indians, the infringement issue is raised. That is, does the state tax infringe upon tribal self-government? The answer might very well be "no" *unless* the tribe also is exercising its taxing authority. The imposition of a tax by a tribe *is* an exercise of tribal self-government. If a state tax, together with the tribal tax, imposes such a burden on the activity or transaction that it is no longer carried on, or is removed from the jurisdiction to avoid the tax burden, then the state tax has certainly interfered with the tribal tax. However, even if the state tax only deprives the tribe of some of its tax revenues, it may infringe on the tribe's right to tax.

As already discussed, the Supreme Court in *Confederated Tribes* held that a state tax does not infringe on the right of a tribe to make its own laws and be governed by them just because it destroys a tribal tax base or makes it impossible for the tribe to impose its own tax. It said that a state tax *could* infringe on the right of a tribe to govern itself in some cases, but that it did not do so in the case of cigarette sales. How could the Court make such a distinction? It said:

Washington does not infringe the right of Reservation Indians to "make their own laws and be ruled by them," *Williams v. Lee*, merely because the result of imposing its taxes will be to deprive the Tribes of revenues which they currently are receiving. The principle of tribal self-government, grounded in notions of inherent sovereignty and in congressional policies, seeks an accommodation between the interests of the Tribes and the Federal Government, on the one hand, and those of the State, on the other. *McClanahan v. Arizona State Tax Comm'n*. While the Tribes do have an interest in raising revenues for essential governmental programs, that interest is strongest when the revenues are derived from value generated on the Reservation by activities involving the Tribes and when the taxpayer is the recipient of tribal services. The State also has a legitimate governmental interest in raising revenues, and that interest is likewise strongest when the tax is directed at off-Reservation value and when the taxpayer is the recipient of state services. As we have already noted, Washington's taxes are reasonably designed to prevent the Tribes from marketing their tax exemption to non-members who do not receive significant tribal services and who would otherwise purchase their cigarettes outside the Reservations.

447 U.S. at 156-57 (citations omitted).

Whether this statement is a reliable guide remains to be seen, but, if it is, it means that in future cases like *Crow Tribe of Indians v. Montana*, 650 F.2d 1104 (9th Cir. 1981), state taxes which hinder tribal taxes will be struck down *if* the tribal taxes raise revenues for essential governmental programs, *if* the subject of the taxes is value generated on-reservation by an activity involving the tribe, *if* the taxpayer is the recipient of tribal services, and *if* the state's interest in the activity is small or nonexistent. The cigarettes in *Confederated Tribes* were not produced on the reservation and therefore were not value generated on the reservation.

Moreover, the non-Indians who were buying the cigarettes were not necessarily recipients of tribal services.

Perhaps a state tax would be held invalid even if the taxpayer were not the recipient of tribal services, so long as the value being taxed was generated on the reservation. As the court said in *Hoopa Valley Tribe v. Nevins*, 881 F.2d 657, 659 (9th Cir. 1989), *cert denied*, 494 U.S. 1055 (1990), "State taxes or regulations that interfere with tribal activities may be preempted if the tribal activity the state seeks to affect involves goods produced on the reservation."

In any event, it is clear from *Confederated Tribes* that the Supreme Court will not protect Indian tribes from state infringement if they are attempting to market *only* a tax exemption. A tribe must show a significant interest in a non-Indian activity or transaction which it seeks to tax in order to preempt a state tax on the same subject.

As we have already seen in *Crow Tribe v. Montana*, the Ninth Circuit Court of Appeals struck down the State of Montana's attempt to apply its severance and gross proceeds taxes to coal mined by non-Indian producers on the reservation, and on an adjoining strip of land which had been ceded by the Tribe to the United States. Much of the ceded strip had been sold to non-Indians before Congress transferred the remainder of the rights to the strip, including much of the underlying mineral rights, back to the Tribe. The trial court originally dismissed the Tribe's 1978 lawsuit challenging the taxes, but the Ninth Circuit Court of Appeals reversed and remanded in 1981, with instructions to the trial court to weigh the competing tribal and state interests. On remand, the trial court again upheld the tax in 1985.

On its second appeal to the Ninth Circuit Court of Appeals, the Tribe won a complete reversal, with the appellate court chiding the trial court for ignoring its previous opinion. The appellate court held that *Confederated Tribes* could not be relied upon to support the tax because this was not a case where the state attempted to tax or regulate something where no on-reservation value was involved. Coal, the court held, is part of the reservation. Relying on the Supreme Court's opinion in *California v. Cabazon Band of Mission Indians*, 480 U.S. 202 (1987), the court noted that in balancing the interests of the Tribe and the state, a Tribe's interest in immunity from state taxation is traditionally strong, while the state's interest in applying its tax is weak. The court held that the Montana taxes infringed on the Crow Tribe's ability to govern the reservation by depriving it of income to run its government. The Supreme Court affirmed the Ninth Circuit Court of Appeals' ruling.

C. ATTEMPTS TO LIMIT TRIBAL TAXING POWER.

1. Introduction. State and local taxes have frequently been attacked on the grounds that they violate the Commerce Clause of the United States Constitution by discriminating against or imposing undue burdens upon commerce among the states. The Commerce Clause empowers Congress "[t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."

The Commerce Clause is actually three clauses in one. These clauses deal with three distinct subjects: foreign commerce, interstate commerce, and Indian commerce. The Foreign

Commerce and the Interstate Commerce Clauses restrict the ability of states to tax goods which move in commerce between this country and foreign countries, and goods which travel from one state to another state or states.

Since the Foreign Commerce and Interstate Commerce Clauses operate as restrictions upon *state powers*, an ordinary reading of its language would indicate that the Indian Commerce Clause also restricts the taxing power of states--in this case the power to impose taxes which discriminate against or impose undue burdens upon commerce with Indian tribes. That, in fact, is its purpose. In *United States v. Forty-Three Gallons of Whiskey*, 93 U.S. 188 (1876), the Supreme Court held that the purpose of the Indian Commerce Clause was to place Indians under the protection of the federal government. Of course, it was the power of states from which they were being protected.

In *Confederated Tribes*, the Supreme Court seemed to agree with the position that the Indian Commerce Clause was designed to protect Indian tribes. It suggested that a state tax might violate the Indian Commerce Clause if it discriminated against or imposed undue burdens on Indian commerce. It indicated that this might happen if a state tax were imposed on commerce between Indians and non-Indians if the commerce had to do with some "reservation generated value."

In *Merrion*, the Supreme Court reiterated this position, saying "[t]o date, . . . this Court has relied on the Indian Commerce Clause as a shield to protect Indian tribes from state and local interference . . . ." 455 U.S. at 153-54.

2. The Indian Commerce Clause Turned Against Indians. Even though the purpose of the Indian Commerce Clause is clearly to *protect* Indian commerce, opponents of tribal taxes have argued that this clause *limits the tribe's power to tax*. This argument was raised in *Merrion*. The non-Indian companies fighting the Tribe's oil and gas severance tax claimed that the tax violated the Commerce Clause because it interfered with interstate commerce. Of course, this argument assumed that a tribal tax *could ever violate* the Commerce Clause, and this became one of the basic issues in the case. Unfortunately, although the case has now been decided by the Supreme Court, this question has not been given a final answer.

The Tenth Circuit Court of Appeals in *Merrion v. Jicarilla Apache Tribe*, 617 F.2d 537 (1980), had held that it was impossible for an Indian tribe to violate the *Interstate* Commerce Clause because that clause applies only to states, and Indian tribes are not states. However, the Court of Appeals *did* hold that it was possible for a tribal tax to violate the *Indian* Commerce Clause, although it found that the oil and gas severance tax in *Merrion* did not, in fact, violate it. The Court of Appeals said that the Indian Commerce Clause *limits* the taxing power of Indian tribes:

We hold the standard to be used in applying that clause is whether a tribe's tax legislation infringes upon the national interest in maintaining the free flow of interstate trade. Our view is that this national interest is measured by traditional analyses.

* * *

[T]his clause of its own force limits the power of the tribes as well as the states.

617 F.2d at 544-45.

When the Supreme Court considered *Merrion*, it also considered whether a tribal tax could *possibly* violate the Commerce Clause but, as mentioned above, decided not to answer the question. What it said was that "reviewing tribal action under the Interstate Commerce Clause is not without conceptual difficulties." That is, tribal taxes do not fit well into an analysis under the Interstate Commerce Clause. Then the Court said that it did not have to answer that question at all because, even if tribal taxes could possibly violate the Commerce Clause, the Jicarilla Apache Tribe's oil and gas severance tax did not do so. This kind of response could be expected: If a constitutional issue is raised in a case, and a court can decide the case without having to decide the constitutional issue, it will always do so. The Supreme Court avoided the constitutional issue saying:

We see no need to break new ground in this area today: even if we assume that tribal action is subject to the limitations of the Interstate Commerce Clause, this tax does not violate . . . that Clause.

455 U.S. at 154. Then the Court demonstrated the Jicarilla tax did not violate the Commerce Clause even if it could. The upshot is that the Supreme Court still has not given a final answer to the Commerce Clause question, or even a very thorough analysis of the meaning and purpose of the Indian Commerce Clause.

However, in spite of its failure to answer the ultimate question, the Court did all but eliminate the issue from those future lawsuits challenging tribal taxes which have been approved by the Secretary of the Interior under Indian Reorganization Act constitutions and ordinances. It accomplished this result in a highly legalistic manner, but one which should be explained. For a proper understanding of what the Court did, it is necessary to look again at the Commerce Clause which empowers Congress "[t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes." A simple reordering of the language of the clause shows that its purpose was to give *Congress* the power to regulate commerce.

The first question which the Supreme Court considered in *Merrion* was "What business does a court have regulating commerce or in saying what a state or an Indian Tribe can or cannot do under the Commerce Clause?" The Court's answer to this question was that *when* Congress has acted to provide the necessary balance, the courts *do not* have any business scrutinizing the validity of a tax as it relates to the Commerce Clause. It said that courts can step in only when Congress has not provided the necessary checkpoints for evaluating the tax. If Congress has acted, then it doesn't matter whether the courts agree with Congress or not. In the case of tribal taxes enacted pursuant to Indian Reorganization Act constitutions and ordinances approved by the Secretary, the Court said that Congress has clearly acted and therefore, there really is no reason why a court should become involved in deciding whether a tribe's tax passes muster under the Commerce Clause. It described how Congress has acted as follows:

Here, *Congress has affirmatively acted by providing a series of federal check-points that must be cleared before a tribal tax can take effect. Under the Indian Reorganization Act, a tribe must*

obtain approval from the Secretary before it adopts or revises its constitution to announce its intention to tax non-members. Further, before the ordinance imposing the severance tax challenged here could take effect, the Tribe was required again to obtain approval from the Secretary.

As we noted earlier, the severance tax challenged by petitioners was enacted in accordance with this congressional scheme. Both the Tribe's Revised Constitution and the challenged tax ordinance received the requisite approval from the Secretary. This course of events fulfilled the administrative process established by Congress to monitor such exercises of tribal authority. As a result, this Tribal tax comes to us in a posture significantly different from a challenged state tax, which does not need specific federal approval to take effect, and which therefore requires, in the absence of congressional ratification, judicial review to ensure that it does not unduly burden or discriminate against interstate commerce. Judicial review of the Indian tax measure, in contrast, would duplicate the administrative review called for by the congressional scheme.

455 U.S. at 155-56 (emphasis added).

The Supreme Court concluded, then, that for cases involving IRA tribes, the issue should not be raised in court since Congress has exercised its prerogative to act, and thereby precluded judicial action. The drawback with the *Merrion* opinion for Indian tribes, however, was the negative implication that taxes levied by non-IRA tribes might be invalid because the federal checkpoints were missing. Indeed this argument was made to a number of courts which, following the Supreme Court's decision in *Merrion*, reviewed taxes of tribes which had elected not to organize and adopt constitutions pursuant to the IRA. In short, the absence of the federal checkpoints which prevented judicial review in *Merrion* seemed to invite judicial review in *Southland Royalty Co. v. Navajo Tribe*, 715 F.2d 486 (10th Cir. 1983), *Conoco, Inc. v. Shoshone and Arapahoe Tribes*, 569 F. Supp 801 (D. Wyo. 1983), and *Kerr-McGee Corp. v. Navajo Tribe*, 471 U.S. 195 (1985). In *Kerr-McGee*, the Supreme Court eliminated doubt about the abilitiy of non-IRA tribes to levy taxes by holding that although Congress may erect "checkpoints that must be cleared before a tribal tax can take effect," Congress has not done so nor has it intended to recognize only tribal taxes authorized by constitutions written under the IRA. *Id*., at 198-99 (quoting *Merrion*).

Over ten years ago the Supreme Court, in a case dealing with state taxes, established the standards for judicial review of a tax to determine whether it infringes upon the national interest in maintaining the free flow of interstate trade. The standards are these: A tax will be sustained against a Commerce Clause challenge when: (1) the tax is applied to an activity with a substantial connection to the taxing government; (2) the tax is fairly apportioned; (3) the tax does not discriminate against interstate commerce; and, (4) the tax is fairly related to the services provided by the taxing government. Challenges regarding the first, third and fourth tests were dealt with in *Southland Royalty Co. v. Navajo Tribe* and *Conoco v. Shoshone and Arapahoe Tribes*.

In *Southland Royalty Co.*, 715 F.2d 486 (10th Cir. 1983), the Tenth Circuit Court of Appeals reviewed and upheld Navajo taxes on non-Indian oil and gas lease interests despite challenges under tests one and three. The court held that the Navajo taxes did not discriminate against interstate commerce because they applied equally to oil and gas severed on-reservation,

whether sold on or transported off the reservation and sold; and that even though both the state and the Tribe imposed taxes, this caused no unconstitutional multiple burden on the taxpayers because the state and the Tribe each had a strong enough connection to the severance of the oil and gas to tax that activity.

In *Conoco*, 569 F.Supp. 801 (1983), the United States District Court in Wyoming upheld a Shoshone and Arapaho severance tax despite challenges under tests three and four. As in *Southland*, the court found that the tax did not discriminate against interstate commerce because it did not distinguish between minerals removed from and those remaining on the reservation. Further, the court said that tribes do not have to go through the paces of taxing themselves, and that individuals' royalty interests should remain exempt under *Squire v. Capoeman*, 351 U.S. 1 (1956), as direct income from trust lands.

The court also held that the tribal tax was fairly related to the services and benefits rendered. It held, as the Supreme Court had in another case when it upheld a Montana severance tax that amounted to 30% of the value of minerals produced, the "general advantages of a civilized society" and the privilege of depleting the resources were sufficient justifications for the tax.

3. Lack of Sovereign Power to Tax. In *Alaska v. Native Village of Venetie*, 856 F.2d 1384 (9th Cir. 1988), the Ninth Circuit Court of Appeals announced a new theory by which tribal taxes may be challenged: assertions that the particular tribe seeking to exercise taxing power lacks the sovereign power to do so. In *Venetie*, the State of Alaska sued the Native Village of Venetie to enjoin it from taxing a contractor working on a state project. The Court of Appeals upheld the trial court's order enjoining the Native Village of Venetie from applying its tax pending a full trial. The Court of Appeals ruled a trial was necessary to determine whether the Native Village of Venetie actually holds sovereign governmental powers. The court was not persuaded by the Native Village of Venetie's assertion that it is a direct successor to an IRA government known as the Village of Venetie. The court also wanted a trial on the issue whether the Native Village of Venetie has sovereign authority over the land in question, inasmuch as it had its reservation status revoked by Congress under the Alaskan Native Claims Settlement Act in 1971, and now holds its land in fee status. The court implied that because the land is not a reservation, the Native Village of Venetie would not have taxing authority unless the land could be considered "Indian country" as a "dependent Indian community." The court also rejected the Native Village of Venetie's argument that it has sovereign immunity from the State of Alaska's suit, and that the state should have exhausted its tribal court remedies before coming to federal court; both of these arguments, the court reasoned, depend in the first instance of the Native Village of Venetie's status as a sovereign government.

4. Federal Preemption of Tribal Power to Tax. The non-Indian taxpayers in *Merrion* argued in the Supreme Court that the federal government had preempted the Tribe's right to impose a tax on them by enactment of a 1927 mineral leasing law which authorized the states to impose the same tax (an oil and gas severance tax) that the Tribe was imposing. The Jicarilla Apache Tribe's Reservation is an executive order reservation. The 1927 federal law authorized states to tax the extraction of minerals from Indian lands on executive order reservations. The Supreme Court said that, even though the state could tax mineral extractions from the reservation under the 1927

law, the Tribe still retained its own right to tax. The Court said that this right had not been preempted by the 1927 law. The non-Indian taxpayers also argued that the 1938 Mineral Leasing Act, which gives the Interior Secretary comprehensive authority to regulate the leasing of mineral rights from Indian reservations, preempted the Tribe's taxing authority because the severance taxes constituted a burden on the non-Indian lessees which was outside the scope of the 1938 Act. The Court held that the 1938 Act did not preempt the Tribe's authority either.

The Court said that the preemption argument is a new one and goes against prevailing thinking: "In *Colville* . . . we concluded that the `widely held understanding within the federal government has always been that *federal law to date has not worked a divestiture of Indian taxing power*'. . . . Moreover, we noted that `[n]o federal statute cited to us shows any congressional departure from this view.'" 455 U.S. at 149 (emphasis added).

The Court found that the non-Indian companies fighting the tax in *Merrion* had not shown the Court any statute "that specifically divests the Tribe of its power to impose a severance tax on their mining activities." *Id.* In this respect the Court said that out of respect for tribal sovereignty it would not find that any act of Congress divests a tribe of its taxing power without a clear showing that Congress intended to restrict a tribe's power to tax. Moreover, it said it is a settled principle of taxation that different sovereigns can tax the same transaction. Therefore, the mere fact that one sovereign may tax the transaction does not exclude other sovereigns from taxing it. The Court found no indication whatsoever in the 1927 Act, in the 1938 law, or in national energy policies. It said:

We find no "clear indications" that Congress has implicitly deprived the Tribe of its power to impose the severance tax. In any event, if there were ambiguity on this point, the doubt would benefit the Tribe, for "[a]mbiguities in federal law have been construed generously in order to comport with . . . traditional notions of sovereignty and with the federal policy of encouraging tribal independence."

Id. at 152.

In holding that the 1938 Act did not preempt the Tribe's authority to impose the severance taxes, the Court noted that the law itself provided that it did not restrict tribes' right to lease lands pursuant to their IRA constitutions and charters. The Court said:

Therefore, this Act does not prohibit the Tribe from imposing a severance tax on petitioner's mining activities pursuant to its Revised Constitution, *when both the Revised Constitution and the ordinance authorizing the tax are approved by the Secretary*.

Id. at 150 (emphasis added).

The Court was probably unaware that its emphasis on secretarial approval would encourage the challenges in the *Kerr-McGee, Southland Royalty Co*. and *Conoco* cases to taxes enacted by tribes who either had no constitutions or whose constitutions did not require secretarial approval of their tax ordinance.

In *Kerr-McGee Corp. v. Navajo Tribe of Indians*, 471 U.S. 195 (1985), the Supreme Court closely examined the IRA and the 1938 Mineral Leasing Act and held that neither required that tribal taxes must be authorized by IRA constitutions or be approved by the Secretary.

The Court reaffirmed that the terms of the IRA do not govern tribes which, like Navajo and Colville, declined to accept its provisions, and held that while a tribe which does choose to adopt a constitution pursuant to the IRA must have it approved by the Secretary, the IRA does not require that constitution to condition tribal taxing power upon secretarial approval.

As to the 1938 Act, the Court held that even though the law provides that all mineral lease operations under the law are subject to secretarial rules and regulations, the law does not require that the Secretary approve tribal taxes. The Court was guided by its duty to "tread lightly" in interpreting less-than-explicit statutes which may interfere with tribal sovereignty. The Court was also greatly influenced by the policy of the federal government to promote tribal self-government, and in that regard referred to policy statements in the Indian Financing Act and to the President's January 24, 1983 Statement on Indian Policy:

[T]he Federal Government is "firmly committed to the goal of promoting tribal self-government." *See, e.g.*, Indian Financing Act of 1974, 88 Stat. 77, 25 U.S.C. § 1451 *et seq.* The power to tax members and non-Indians alike is surely an essential attribute of such self-government; the Navajos can gain independence from the Federal Government only by financing their own police force, schools, and social programs.

Kerr-McGee Corp. v. Navajo Tribe, 471 U.S. 195, 200-201 (1985) (citations omitted) quoting *New Mexico v. Mescalero Apache Tribe*, 462 U.S. 324 (1983).

5. Contract Limitations. In *Merrion v. Jicarilla Apache Tribe*, the lease between the Tribe and the non-Indian lessees had a provision that the "royalty or annual rental" under the lease would not be increased without the written consent of the parties. The lessees argued that the tax imposed by the Tribe increased the royalty or annual rental. The Court of Appeals said that such a contract provision does not preclude a sovereign government, which is also a lessor, from imposing a tax, which has the practical effect of increasing revenues, unless the contract so provides. The Court of Appeals said:

It is well settled that such an agreement does not prevent the exaction of a license tax "unless this right has been specifically surrendered in terms which admit of no other reasonable interpretation."

617 F.2d at 549 (citations omitted).

The Supreme Court in *Merrion* cited this very language of the Ninth Circuit Court of Appeals in responding to this argument. In the Supreme Court, however, the argument was made somewhat differently than in the Court of Appeals. It went like this: the Tribe's power to tax non-Indians is derived solely from its power to exclude them from the reservation. Once the Tribe entered into a lease with non-Indian companies to extract oil and gas from the reservation the Tribe gave up the right to exclude them from the reservation. In doing so, it gave up the derivative right to tax them.

As we have already seen, the Court rejected this argument, holding that the Tribe's power to exclude nonmembers from the reservation is not the sole source of its power to tax them. Rather, tribes have the authority to impose taxes as part of their power to govern and pay for the costs of self-government. The Court said, however, that even if the power to exclude were the sole source of the Tribe's power to tax, the Tribe would not lose the power to tax merely by entering into a lease which permitted a non-Indian to enter and remain on tribal land. It said that in such a case the Tribe still retains its power to place other conditions on the non-Indian's conduct or continued presence on the reservation, including the requirement that he pay taxes. It said that it is a mistake to think of the tribal power to exclude or the derivative authority to tax:

[A]s merely the power possessed by any individual landowner or any social group to attach conditions, including a "tax" or fee, to the entry by a stranger onto private land or into the social group, and not as a sovereign power.

455 U.S. at 146. The power to tax, it explained, is sovereign in nature and is not as easily given up as a private landowner's right to control access to his property. It added that other sovereignties, such as federal, state, and local governments do not waive their sovereign power simply because they enter into contractual relationships:

Contractual arrangements remain subject to subsequent legislation by the presiding sovereign . . . . Without regard to its source, sovereign power, even when unexercised, is an enduring presence that governs all contracts subject to the sovereign's jurisdiction, and will remain intact unless surrendered in unmistakable terms.

Id. at 147-48.

6. Due Process: Taxation Without Representation.

a. The Old Argument. It is regularly argued that tribal taxes on non-Indians violate due process because the non-Indians bear the burden of the tax without being able to exercise other civil liberties such as voting, jury duty, and holding elected office. The Indian Civil Rights Act of 1968 protects non-Indians, as well as Indians and contains a due process clause.

b. The Answer. However, as the Court of Appeals in the *Merrion* case said, the national interest in preventing the deprivation of property without due process becomes involved in taxing "only in the extremely rare case in which the taxing power is so abused the result is, in reality, not a tax, `but constitutes, in substance and effect, the direct exertion of a different and forbidden power, as, for example, the confiscation of property.'" 617 F.2d at 542 (citations omitted).

c. Indian Tribes are Unique. In addition, the Supreme Court has long recognized that Indian tribes are unique and that there is a national interest in preserving them. As the Court stated in *Morton v. Mancari*, 417 U.S. 535 (1974), Indian tribes are unique governmental entities with a special, constitutionally-established trust relationship with the United States. The rights of tribal members are not based upon race, but upon constituency, that is, upon membership in a quasi-sovereign federally-recognized Indian tribe. It would clearly injure the national interest in preserving the cultural identity of Indian tribes if non-Indians were allowed to take the same part in tribal government as Indians.

d. The Indian Civil Rights Act. Thus, although the Indian Civil Rights Act protects non-Indians as well as Indians and contains a due process clause, it is unlikely that it could be used to defeat a tribal tax.

7. Equal Protection.

a. Taxes Applied Equally to Indians and Non-Indians. A tax which applies equally to Indians and non-Indians on the reservation would obviously treat both groups equally.

b. A Tax On Non-Indians. A tax only on non-Indians, or a tax which burdens non-Indians more heavily than Indians, raises an "equal protection" issue. There are serious questions involved with such a tax. An unequal tax might survive if carefully drawn and rationally related to some important purpose which requires giving Indians a special advantage. But *any unequal tax* requires extremely careful analysis of legal rights as well as expert draftsmanship. Equally important, a tribe should consider the political wisdom of a tribal tax which discriminates against non-Indians.

As a practical matter though, it is simply not necessary to draw a tax which, on its face, discriminates against racial or political groups. Since a government can tax a wide variety of activities, transactions, and property rights, it can choose to levy its taxes where they are most likely to raise revenue and least likely to fall on those who cannot afford to pay. Carefully selecting activities, transactions, and property interests for taxation can eliminate the need to draw taxing lines on the basis of race or tribal affiliation.

An example was considered in *Southland Royalty Company v. Navajo Tribe*, 715 F.2d 486 (10th Cir. 1983), which involved a tribal tax on the value of mineral interests and on gross receipts. The tribal tax ordinance provided a standard deduction of $125,000, thereby excluding all Navajo-owned business from the tax and leaving the oil companies to bear the entire tax burden. The oil companies attacked the ordinance on the ground of equal protection, and the Tenth Circuit Court of Appeals noted that the ordinance had not yet been put into operation and that it would, therefore, be premature to consider the equal protection issue.

Another example was considered by the district court in *Conoco v. Shoshone and Arapaho Tribes*, 569 F. Supp. 801 (D. Wyo. 1983). There, the Tribe's oil and gas severance tax did not apply to the oil and gas interests of the Tribe or tribal members. The oil company argued that the tax was discriminatory. The district court disagreed, stating that there was no reason why tribes must "go through the paces of taxing themselves." Further, the royalty interests of individual tribal members were properly exempt from taxation under the rule of *Squire v. Capoeman*, 351 U.S. 1 (1956).

It is well-known that after governments collect tax revenues they *redistribute* them to those sectors of the economy that they think should have them. Redistribution of wealth is a legitimate function of government. Therefore, even if a tribe enacts a tax which falls generally on its members, as well as upon non-members, this need not be the end of the matter. If a tribe has a goal of improving the living standards of its members, the revenues it collects in taxes can be redistributed through tribal programs benefitting tribal members, even those who have had to pay

taxes. In this manner it may shift the economic benefits of its taxing program to tribal members while taxing Indians and non-Indians alike.