Why Beggar Thy Indian Neighbor?

The case for tribal primacy in taxation in Indian country

Kelly S. Croman & Jonathan B. Taylor

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Discussion Draft
Send comments to:
kscroman@gmail.com & jonathan@taylorpolicy.com

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About the Authors

Kelly Croman is Chair of the National Intertribal Tax Alliance and Director of the Office of Tribal Attorney for the Confederated Tribes of the Chehalis Reservation. She formerly served as CEO of Island Enterprises, Inc., the economic development arm of the Squaxin Island Tribe; General Counsel for Marine View Ventures, Inc., the economic development arm of the Puyallup Tribe; and tribal attorney for the Squaxin Island Tribe.

Jonathan Taylor is President of the Taylor Policy Group, an economics and public policy consultancy; a Research Affiliate at the Harvard Project on American Indian Economic Development at the Kennedy School of Government; and a Senior Policy Associate at the Native Nations Institute, Udall Center for Studies in Public Policy, University of Arizona, Tucson.

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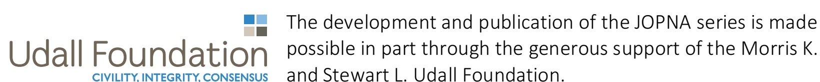

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Abstract

The law governing taxation in Indian country is a mess. The accretion of common law precedents and the general tendency of states to assert primacy over the taxation of non-Indians create absurd outcomes. This article makes the case three ways. The argument based on the law shows that particularized, fact-specific precedents create a thicket of rulings that impede business development. The argument based on facts shows that these impediments to economic development harm not only tribal economies, but state and local economies, too. And the argument based on just claims testifies to the fact that the current arrangement could hardly have emerged from the actions of willing and informed governments operating in good faith. To borrow from Adam Smith, states beggar their Indian neighbors, seeking fiscal gain to the tribes' detriment and, ultimately, their own. We conclude by recommending actions to bring fairness and certainty to the law governing taxation in Indian country.

I. Introduction

> 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....[It derives] from the tribe's general authority, as sovereign, to control economic activities within its jurisdiction, and to defray the cost of providing governmental services by requiring contributions from persons or enterprises engaged in in such activities. (*Merrion v. Jicarilla*, 1982, p. 130)

This language, from a 1982 U.S. Supreme Court decision, underscores two important concepts. First, taxation is an important instrument of control; and second, taxation finances governmental functions. An infringement upon the right to tax infringes upon both core attributes of sovereign governance.

Every government relies on tax revenues to fund essential services and public goods, including building and maintaining infrastructure (such as roads, broadband, water, and wastewater systems); permitting and licensing businesses and professions; enforcing contracts and resolving disputes; ensuring public safety; educating children and workers; enforcing building codes and other safety measures; insuring against unemployment and worker injury; and more. Tax revenues are used as well for natural resource and environmental protection, parks and recreation, housing, community development, and assistance to disabled and needy citizens. Governments also design taxes and tax exemptions to encourage behaviors in the public interest, such as smoking cessation, economic investment, pollution reduction, and home ownership.

While the rights of tribes to impose taxes are well established, states usually insist on primacy when jurisdictions overlap. The ad hoc accretion of precedents resulting from litigation over such overlap creates bizarre constraints on tribal governments' ability to raise revenue and direct activity in their jurisdictions. This infringement diminishes the sovereignty of tribal

governments, diminishes government services and public goods for tribal citizens and others, and encumbers states, local governments, and their respective citizens.

Our purpose here is to demonstrate that as a legal and economic matter, Indian tax policy is deeply flawed and must be changed. Our arguments are presented in three categories: legal (*de jure*), practical (*de facto*), and moral (*de recto*).[1] The *de jure*[2] argument demonstrates how court precedents have made a complex and often absurd mess of what should be a relatively straightforward body of law. The *de facto*[3] argument documents the deleterious consequences of those precedents for Indian *and* non-Indian economies. The *de recto*[4] argument explores the moral case for Indian tax reform, a case based on just claims. The final section of the paper offers recommendations. Many of the examples below are from Washington State, but our findings have implications across all the states wherein Indian country[5] is found, so we have also included examples from farther afield.

II. THE *DE JURE* CASE FOR CHANGE

Fundamentals of Good Tax Policy Are Long-Established Outside Indian Country

From *The Federalist Papers* of 1787 to modern publications of the American Institute of Certified Public Accountants and the National Conference of State Legislatures, there is a shared understanding that tax systems ought to at least:

- Reliably provide sufficient governmental revenues;
- Provide certainty; and
- Promote economic growth and efficiency.[6]

These principles are mutually reinforcing. Certainty reduces financial and practical barriers to economic growth and promotes efficiency. Growth and efficiency provide a larger tax base and

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[1] Credit goes to Joseph Kalt and Joseph Singer (2004) for introducing us to this tripartite framework.

[2] "*de jure*...[Law Latin 'as a matter of law'] Existing by right or according to law" (Garner, 2004, p. 458).

[3] "*de facto*...[Law Latin 'in point of fact'] 1. Actual; existing in fact; having effect even though not formally or legally recognized" (Garner, 2004, p. 448).

[4] We adopt Kalt and Singer's formulation of *de recto* as "by moral principle or right" (2004, p. 6).

[5] "[T]he term 'Indian country'…means (a) all land within the limits of any Indian reservation under the jurisdiction of the United States Government, notwithstanding the issuance of any patent, and, including rights-of-way running through the reservation, (b) all dependent Indian communities within the borders of the United States whether within the original or subsequently acquired territory thereof, and whether within or without the limits of a state, and (c) all Indian allotments, the Indian titles to which have not been extinguished, including rights-of-way running through the same." (18 USC §1151).

[6] For example, by addressing market failures and underwriting public goods or, barring that, by minimally distorting incentives. See, e.g., Smith's *Wealth of Nations* (1776), Hamilton's *Federalist Papers* Nos. 30–36 (1961), the National Conference of State Legislatures' *Tax Policy Handbook* (2010), the American Institute of Certified Public Accountants' *Guiding Principles for Tax Equity and Fairness* (Swingen, 2007), Musgrave & Musgrave (1984, p. 224), Rosen & Gayer (2010, chapter 16), and many others.

improved compliance, thus helping to ensure sufficiency and reliability of revenues. And an effective income-generating system reduces the need for governments to frequently alter tax codes, reinforcing certainty.

Concurrent jurisdiction—the authority of more than one jurisdiction to tax the same property, activity, or transaction—complicates the application of these principles. It can reduce certainty for both taxpayers and governments. It can impede economic growth when it results in excessive taxation. More important for our analysis here, it can diminish a government's powers or even effectively strip them away.

If one government occupies the field, the other government cannot fully exercise its authority to tax without driving residents and businesses from its jurisdiction.[7] This is an old problem—one recognized in the jurisprudence of interstate commerce:

> Multiple taxation is to be avoided with respect to interstate commerce by apportionment so that no jurisdiction may tax all the property of a multistate business, and the rule of apportionment is enforced by the Supreme Court with jurisdiction over all the states. (Congressional Research Service, 2014, p. 272)

Equitably apportioning tax authority was somewhat simpler in the country's early years than it is today.[8] The devolution of responsibilities to state and local governments complicates the task of making sound tax policy at a given level of government while also minimally distorting economic activity elsewhere in the federal system (National Conference of State Legislatures, 2007; P. E. Peterson, 1995). As tribal governments exercise more of their authority and interact more frequently with all three levels of government in the federal system, achieving inter-jurisdictional equity becomes more challenging still. States and counties owe at least the deference they offer other state and local governments to tribal governments, which must also provide services, need revenue, and are recognized as sovereign in the US Constitution.

But at best, federal, state, and local policymakers overlook tribal governments. Sometimes that is intentional, as when a non-tribal government views Indian country as a potential source of revenue rather than as a polity with inherent public finance requirements. "Outdated and inaccurate perceptions of American Indian tribes continue to prevail in non-Indian communities and state officials may not understand that tribes are functioning governments" (Johnson, Kaufmann, Dossett, Hicks & Davis, 2009, p. 1). Even where tribal governments might be

[7] Many countries have addressed these issues through tax treaties to eliminate double taxation. See, e.g., McIntyre (n.d.).

[8] "The framers of the Constitution envisioned a concurrent tax system where certain public services, such as defense and transportation infrastructure, were funded at the federal level and other items, such as education and public safety, were funded at the state and local level." (Swingen, 2007, p. 9) See also Hamilton's *Federalist Paper* No. 32 (1961).

acknowledged, non-tribal policymakers regularly fail to adequately understand or incorporate tribal fiscal prerogatives in striking fair tax apportionments.[9]

At worst, state and local governments deprecate the power of tribes to set tax rates. Fair apportionment implies that governments have commensurate powers to offer tax incentives. State and local governments use tax policy to entice customers and firms to transact within their jurisdictions. A company's threat to depart (or not to locate in) a jurisdiction may give rise to an abatement race subject to the winner's curse: The biggest tax cutter wins the business but garners meager or nonexistent net fiscal benefits. As the National Conference of State Legislatures observes, "Any state that imposes a tax burden far different from that of its neighboring states runs the risk of hurting its economy" (2007, p. 5). Whether or not such mechanisms are advisable, the use of tax incentives is so common among all levels of government that denying this tool to one government while allowing it for others undercuts fair apportionment. Nonetheless, tribes routinely confront political hostility or litigation from jurisdictions with higher taxes.

In a complex global economy in which all governments are struggling with increasing competition, costs, and responsibilities, maintaining a tax system that satisfies the fundamental principles articulated above is challenging. The challenge is amplified in Indian country, where, as we will show:

- Federal law limits tribes' revenue options;
- Indian tax law creates uncertainty;
- Principles of fair apportionment are not generally applied; and
- Indian tax law is economically inefficient and inhibits growth.

What is the norm throughout the country is turned on its head in Indian country.

Federal Law and Related Practical Challenges Limit Tribes' Revenue Options

Tribal governments provide public goods and services similar to those provided by state and federal governments. They manage forests and fisheries, generate electricity, monitor air and water quality, operate schools and colleges, build and maintain roads and bridges, provide health care, operate correctional facilities, and assist families in poverty. They also have responsibilities resembling those of county and municipal governments: They maintain sewer lines, police neighborhoods, provide emergency services, teach children, remove snow, provide transit services, maintain parks, collect trash, conduct elections, maintain cemeteries, and provide public housing.

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[9] The National Conference of State Legislatures has produced a very thoughtful document titled *Government to Government: Models of Cooperation between States and Tribes* (Johnson et al., 2009) in furtherance of its efforts to assist tribes and states to cooperatively address mutual interests for the benefit of citizens of both. The same organization, however, produces other publications on tax policy and equity that never mention tribal governments.

Tribal governments have to perform these functions in a legal environment that deprives them of the usual means of raising government funds. "Tribal governments have extreme difficulty in raising revenue; they have virtually no tax base" (Fletcher, 2004, p. 771). Property taxes are a significant source of revenue for most state and local governments.[10] Tribal governments, however, may not impose a real property tax on trust lands, which are owned by the federal government. Depending upon the reservation, trust acreage may reach 100% of a tribe's land base. Meanwhile, in most jurisdictions, tribal governments and their citizens *are* subject to state property taxes on fee lands, even within reservation boundaries, absent an exemption under individual state laws (*County of Yakima v. Yakima Nation*, 1992).[11] This important and stable source of revenue is thus often wholly unavailable to tribal governments, and tribes must look elsewhere.

Income taxes are impractical, too. Given that reservation per capita incomes are less than half the US average (Akee & Taylor, 2014), proportionally more Indians qualify for negative income taxes (principally the Earned Income Tax Credit), effectively precluding tribes from using this common and robust revenue source.

As we will describe, states generally cannot impose taxes where the legal incidence falls on tribes, their citizens, and their enterprises. This seemingly creates an opportunity for tribes to impose, say, a sales tax without creating an excessive burden. But taxing only the portion of the reservation economy that is immune from state and local taxes would be impractical. Imagine if West Virginia or California could tax only native-born residents. The analogy is imperfect, but the administrative complexity would be about the same. As for tribe-owned businesses, the power to tax is moot: The profits already accrue to the governments that own them. A tribal tax that reduced those profits would alter the accounting of those government revenues but not increase them.

Insufficient tax revenues make tribal treasuries more dependent than they would like to be on federal transfers, which are widely acknowledged to be inadequate (US Commission on Civil Rights, 2003), and on tribe-owned enterprises, which bring numerous challenges.[12]

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[10] In the US, "[p]roperty taxes were the most prominent source of state and local tax revenues in fiscal year 2010" (Malm & Kant, 2013).

[11] For fee land allotted under acts other than the General Allotment Act, the courts disagree. In the Ninth Circuit, the court held that the Lummi Indian Nation's fee patented reservation land was not exempt from *ad valorem* taxes imposed by Washington State, despite the fact that the land was allotted under the Treaty of Point Elliot, not the General Allotment Act. (*Lummi Indian Tribe v. Whatcom County*, 1993). The Sixth Circuit and the Crow Tribal Court have reached the opposite conclusion (*Pease v. Yellowstone*, 1994; *United States v. Michigan*, 1997).

[12] The gross product of Indian country continues to be heavily government-owned even as the global economy is less and less so, despite the better pricing, productivity, and profitability provided by private ownership (Grant & Taylor, 2007; Megginson & Netter, 2001). Moreover, in contrast to the relatively modest collection costs of taxation, developing ample dividends from tribal enterprises requires substantial capital investment or, barring that, steady management over long time horizons so that growth compounding can do its work.

Consequently, tribes are hobbled in their competition with other governments—not only in the domain of taxation, but also in public goods and services offered.[13]

Indian Tax Law Creates Uncertainty

Put simply, Indian tax law is a mess.

Although some basic principles of federal Indian tax law are well established, the field is rife with gray areas. As Justice Rehnquist observed thirty-five years ago,

> Since early in the last century, this Court has been struggling to develop a coherent doctrine by which to measure with some predictability the scope of Indian immunity from state taxation. (*Washington v. Colville*, 1980, p. 176)[14]

A recent 320-page journal article attempts to make sense of the inconsistencies but concludes that the thicket has yet to be cleared:

> Case-by-case adjudication by a court is a notoriously difficult way of imposing order and coherence on a body of doctrine....The Supreme Court has not distinguished itself, mischaracterizing the tax before it, abusing precedent, lapsing into *ipse dixit*[15] reasoning, misreading or ignoring history, and retreating into formalism. (Pomp, 2010, pp. 1220–21)

Settling what should be basic questions requires nuanced, fact-specific analysis. Not only is slow and costly litigation common, but it rarely leads to comprehensive, predictable, or transferrable solutions to the issues that arise between tribes and neighboring state and local governments. Court rulings in Indian tax litigation regularly create more uncertainties than they resolve, because inconsistent decisions so often arise when disparate courts review case-specific facts.

Even where clear rules exist, the law quickly becomes complicated, because the determinative question in many Indian tax cases is not Where did the transaction occur? but Who bears the legal incidence of a state tax? The principle that, absent an express congressional statement to the contrary, a state may not impose taxes on an Indian tribe or its members in Indian country (*Oklahoma Tax Commission v. Chickasaw Nation*, 1995, pp. 458–9) ostensibly works in the tribes' favor. Local governments, as political subdivisions of the states, are similarly proscribed. As a result, businesses owned and operated by tribes and their citizens in their own Indian country will generally be free of state and local taxes such as business, manufacturing,

[13] Governments compete in the tax abatement races familiar to newspaper readers (such as to attract a new Tesla factory to Nevada or Texas) *and* across the whole bundle of public goods, services, taxes, and fees. *Tiebout competition* (1956) describes the process whereby citizens vote with their feet to accept or reject local governments' offerings (e.g., school quality or infrastructure) and prices (taxes and fees). The sorting of citizens into communities of similar preferences and willingness to pay for government services has been empirically confirmed across a wide variety of US contexts (Mueller, 2009, pp. 199–202).

[14] Rehnquist was concurring in part, concurring in the result in part, and dissenting in part.

[15] "*ipse dixit*...[Latin 'he himself said it'] Something asserted not proved" (Garner, 2004, p. 847).

and sales taxes. This principle of federal Indian law has also been held to bar states from taxing the personal property of tribes and their members in Indian country (*Bryan v. Itasca County*, 1976; *Moe v. Confederated Salish & Kootenai Tribes*, 1976; *Oklahoma Tax Commission v. Sac and Fox Nation*, 1993). The rule is simple to articulate, but verifying where the legal incidence of a tax falls, and which individuals and transactions are entitled to an exemption, is complex.

Similarly clear is the precedent that if the legal incidence of a state tax falls on a non-Indian—even on activity within Indian country—the state can generally impose its tax (*Oklahoma Tax Commission v. Chickasaw Nation*, 1995, p. 459). However, exceptions to this general rule that empower tribes to preempt state taxation are complex and inconsistently applied. At first glance, the exceptions appear simple and certain. If the tax is preempted by federal law, or if it interferes with a tribe's ability to exercise its sovereign functions, it *does not* apply to non-Indians in Indian country (*Ramah Navajo Sch. Bd. v. Bureau of Revenue of NM*, 1982, p. 837; *White Mountain Apache Tribe v. Bracker*, 1980, p. 142). Either exception can be sufficient basis for invalidating a state tax imposed on non-Indians, but the two barriers are usually analyzed together and sometimes conflated (*Ramah Navajo Sch. Bd. v. Bureau of Revenue of NM*, 1982, p. 837; *White Mountain Apache Tribe v. Bracker*, 1980, p. 143). In the relatively rare instances where federal law explicitly prohibits application of a tax in Indian country, it trumps state law. But more broadly, outcomes have been inconsistent and confusing because courts have delved into nuanced and fact-specific analyses that arise from federal regulatory schemes or preemption analyses—"balancing tests"—used to determine whether the combined federal and tribal interests outweigh the state's interests (*Gila River Indian Community v. Waddell*, 1992; *Gila River Indian Community v. Waddell*, 1996; *New Mexico v. Mescalero Apache Tribe*, 1983; *Yavapai-Prescott v. Scott*, 1997).

These balancing tests have arisen because of the court's holding that there is "no rigid rule by which to resolve the question whether a particular state law may be applied to an Indian reservation or to tribal members" (*White Mountain Apache Tribe v. Bracker*, 1980, p. 142). The test is meant to reflect

> [t]he tradition of Indian sovereignty over the reservation and tribal members… reflected and encouraged in [federal statutes] demonstrating a firm federal policy of promoting tribal self-sufficiency and economic development. (*White Mountain Apache Tribe v. Bracker*, 1980, p. 143)

Under this "*Bracker* analysis," tribal and federal interests in an activity are weighed against state interests. If the balance favors the state, it may impose its tax and may also impose minimal burdens on the tribe or its members to assist in collecting the tax.[16] Otherwise, the state tax on the non-Indian is preempted.

[16] Consider, however, whether a non-Indian retailer would deem it a "minimal burden" to be required to confirm the citizenship of all purchasers at the register and to collect and remit taxes to a neighboring jurisdiction on the basis of the citizenship of those purchasers, when the products subject to tax and the tax rates on those products differed in the two jurisdictions. Indian law precedents allow states to impose that burden on tribes in their own Indian country.

Preemption cases are extremely fact-specific, and accreted inconsistent holdings strengthen incentives for state and local governments to litigate. Contrast, for example, *White Mountain Apache v. Bracker* (in which the Supreme Court found that federal regulation of Indian timber is "comprehensive" and, therefore, Arizona's motor-carrier license tax and fuel taxes could not be applied to a non-Indian company working under contract with a tribal corporation) with *Cotton Petroleum Corp. v. New Mexico* (1989), (in which the Court upheld the simultaneous imposition of state and tribal severance taxes on a non-Indian company extracting oil and gas on Jicarilla trust lands). Federal regulation of both trust resources—timber and minerals—is comprehensive, and in both cases resource revenues constituted the largest source of tribal government revenue. The two cases cannot be reconciled,[17] making it difficult to predict outcomes in balancing test cases.

In essence, *Bracker* balancing puts courts in the position of converting questions in shades of gray—tribal and federal versus state interests—into answers of black or white: The state is or is not preempted. Vague standards regarding improper state interference in tribal self-government compound the challenge, especially when courts conflate this analysis with the weighing of interests rather than analyzing interference as a separate basis for preemption. And additional uncertainty arises because varying case-by-case adjudication determines practical tribal taxing capacity, not a constitutional, statutory, or regulatory articulation of powers. The harm done to tribal *and state* governments and their citizens by unpredictable and incoherent tax policy is real: Dollars and time are wasted, resources go untapped, government-to-government relationships fester and break down, and absurdities in business development practices prevail (as we will show below). Economic development that should occur does not.

Principles of Sound Apportionment Are Not Generally Applied to Indian Country

Generally, outside Indian country, state and local governments cannot tax individuals and businesses making purchases and doing business in other jurisdictions except in those few cases where a use tax applies.[18] For example, Massachusetts cannot generally tax purchases by Massachusetts residents in sales-tax-free New Hampshire. Even where a use tax applies, collection and enforcement are extremely limited for practical reasons.[19] However, under most circumstances state and local governments *are* free to tax non-Indians in Indian country without regard to the existence of a tribal tax system or the principles of sound apportionment (*Moe v. Confederated Salish & Kootenai Tribes*, 1976; *Oklahoma Tax Commission v. Potawatomi Tribe*,

[17] "The Court's analysis [in *Cotton*] fails to recognize the opposite outcomes of *Cotton Petroleum* and *Crow Tribe*, and, indeed, reconciling these two outcomes would be difficult." (Alexander, 1997, p. 399)

[18] In Washington State, for example, use tax is due on goods purchased in another state that has no sales tax or a sales tax lower than Washington's, but only when those goods are purchased for use in Washington. The burden of reporting and remitting the use tax is on the taxpayer (Washington State Department of Revenue, 2010).

[19] Many states require consumers to report their use tax liabilities on their income tax returns, but compliance is less than 1 percent in many states and only 10 percent in the most compliant state (Agrawal & Mardan, 2015, p. 1). According to a May 2014 study by the Washington State Department of Revenue, "Washington border counties will lose $3 billion in taxable retail sales to casual cross-border evasion in Fiscal Year 2014. This represents $193 million in state and $54 million in local sales tax revenues lost to evasion, $247 million in total" (Washington State Department of Revenue, 2014b, p. 1).

1991; *Washington v. Colville*, 1980). This is a significant departure from prevailing practice and introduces a double bind. A tribe seeking to raise revenue from the businesses and individuals to which it provides goods and services must weigh the effect of adding its own taxes to state and local taxes (thereby discouraging much-needed economic activity) against the consequences of not raising the revenue. The double bind frustrates tribal leaders. President Peterson Zah of the Navajo Nation observed in congressional testimony:

> "[D]ouble taxation interferes with our ability to encourage economic activity and to develop effective revenue generating tax programs. Many businesses may find it easier to avoid doing business on our reservations rather than…bear the brunt of an added tax burden…." (as cited in *Michigan v. Bay Mills Indian Community*, 2014)

And the double bind has been noted as a significant obstacle by federal officials. In promulgating leasing regulations, the Secretary of the Interior performed a "comprehensive analysis…showing how tribal interests are affected by state taxes on leases of restricted Indian land" (*Seminole Tribe of Florida v. State of Florida*, 2014, p. 4):

> [T]he Secretary detailed the practical reality…that "the very possibility of an additional State or local tax has a chilling effect on potential lessees as well as the tribe that as a result might refrain from exercising its own sovereign right to impose a tribal tax to support its infrastructure needs." (citing Bureau of Indian Affairs, 2012, p. 72448; *Seminole Tribe of Florida v. State of Florida*, 2014, pp. 5–6)

While fair apportionment is recognized as a fundamental principle of good tax policy at the national and state levels, state and local governments aggressively protect their tax primacy in Indian country.

Indian Tax Law Is Economically Inefficient and Inhibits Growth

As described above, the fundamental principles of good tax policy are generally absent in Indian country. Lacking reliable and sufficient tax revenues, tribal economic development is often inefficient and sometimes completely inhibited.

Legal uncertainty and the time and financial costs of litigation motivate tribes to structure their economic ventures in the manner most likely to win a tax case or to limit the ability of the state to enforce its tax, rather than in the manner that makes the best business or policy sense for the tribe. For their part, non-Indian investors and partners are rarely willing to endure the expense and delay of obtaining certainty on taxation in Indian country.[20] Tax rulings can be obtained from many state taxing agencies, but they are fact-specific and dependent on

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[20] "Indian reservations have to compete with other venues to attract economic activities. To be successful, tribes must offer investors the opportunity to earn economic returns commensurate with the returns they might earn elsewhere. Investment dollars have to come from somewhere. Investor risk is raised if there is uncertainty in tax and regulatory policies that apply to on-reservation business or transactions." (Atkinson & Nilles, 2008, pp. I–2)

notoriously variable case law underpinnings or on the terms of negotiated state-tribal compacts with expiration dates that may not afford the investor sufficient security over the life of the project. The choice of business structure—a fundamental consideration for investors and partners—also has significant tax implications for tribes (Atkinson & Nilles, 2008). Even when a tribe ultimately prevails, litigation is often necessary to establish state tax exemption or tribal preemption whenever a non-tribal partner or investor is involved.

The Great Wolf Lodge case is a good example of both the lack of certainty in Indian law and the creation of perverse incentives. The Confederated Tribes of the Chehalis Reservation formed a Delaware LLC with Great Wolf Resorts, Inc. in which the Tribes had 51% ownership. The LLC constructed and operates a resort, conference center, and water park on lands held in trust for the Tribes under a lease approved by the Bureau of Indian Affairs (*Chehalis Tribes v. Thurston County*, 2013, p. 1154). The Tribes and their partner took great pains to structure a business deal in 2005 to minimize uncertainty regarding the application of state and local taxes. As extra insurance, the Tribes obtained a ruling in 2007 from the Washington State Department of Revenue establishing exemption from state tax. But county officials began assessing property taxes that year, and the Tribes filed suit in 2008. Not until 2013, and after significant expense by all parties, was the dispute finally resolved in the Tribes' favor (*Chehalis Tribes v. Thurston County*, 2013).

Ultimately, the Ninth Circuit decided the case on a very narrow issue related to a specific provision of a federal statute,[21] but along the way the courts examined the smallest details of the deal's structure, financing, and operations—details that the Tribes and its partner had negotiated at the outset in an attempt to avoid just such a dispute. Notwithstanding the Tribes' legal victory, the Washington Department of Revenue added to the uncertainty by issuing temporary guidance that contradicted the clear ruling of the court, only to reverse course in 2014 (Washington State Department of Revenue, 2014a).

Even when legal results are superficially similar, they can mask variation in legal reasoning, which then raises the cost of doing business in Indian country. The water park at Great Wolf Lodge, for example, has three distinct tax characterizations. As stated above, the Ninth Circuit ruled that whether the permanent improvement was owned by a non-Indian or an Indian did not matter—the state property tax was preempted by federal law on the basis of the land status. The Thurston County Board of Equalization ruled on whether the furniture and equipment were taxable, finding that the LLC was a tribal entity and thus, under federal law, immune from the county's personal property taxes. The Washington Department of Revenue ruled on the issue of whether state sales tax applied to non-Indian customers at the water park. It found that the LLC was non-Indian (i.e., subject to tax), yet used the balancing test to rule that "all of the Washington state sales and use taxes are exempted under federal preemption."[22] One set of

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[21] "At issue in this case is whether state and local governments have the power to tax permanent improvements built on non-reservation land owned by the United States and held in trust for an Indian tribe. Pursuant to 25 U.S.C. § 465, and *Mescalero Apache Tribe v. Jones*, 411 U.S. 145 (1973), we hold that they do not." (*Chehalis Tribes v. Thurston County*, 2013)

[22] Washington State Department of Revenue Letter Ruling, February 27, 2007.

business facts produced three similar legal results (the tax was preempted), but the analytical premises were not even close. Though the Tribes were no doubt gratified to have three favorable outcomes (a rare enough occurrence in Indian tax law), the thicket of rationales means that future Indian business deals have more needles to thread.

Sometimes the outcome is even worse than a delayed or byzantine deal—it is an uneconomic one. The tax status of Indian land, and failure to observe apportionment principles, are at the root of the problem. As Justice Sotomayor observed in a recent concurring opinion:

> If non-Indians controlled only a small amount of property on Indian reservations, and if only a negligible amount of land was held in fee, the double-taxation concern might be less severe. But for many Tribes, that is not the case. History explains why this is so: Federal policies enacted in the late 19th and early 20th centuries rendered a devastating blow to tribal ownership.... Indeed, by 1934, the amount of land that passed from Indian Tribes to non-Indians totaled 90 million acres…[and] [s]ixty million acres of land passed to non-Indian hands as a result of surplus programs. These policies have left a devastating legacy, as the cases that have come before this Court demonstrate. (*Michigan v. Bay Mills Indian Community*, 2014)

In stark contrast to the general practice whereby governments with overlapping jurisdiction apportion their tax powers, no such rule or practice exists in federal Indian law. Indeed, Indian land status adds even more complexity. While states may generally tax non-Indians anywhere, including in Indian country, tribes may impose taxes on non-Indians only on trust land (or on fee land within Indian country where they have a consensual relationship with the taxpayer). This adds a strong geographic component to Indian tax law, which results in site selections based not primarily on infrastructure, access, size, and other commercial attributes but on trust status.

Imagine, for example, that a tribe is considering two parcels of land within its reservation for development of a store selling products manufactured by the tribe. The tribe's strategic goal is to tax sales to customers in support of public goods and infrastructure. The first parcel, owned by the tribe in fee, is located on a busy intersection with good visibility and parking. The second parcel, held in trust for the tribe, is six miles from the nearest intersection, at the end of an unpaved tribal road. If the tribe opens its store on the fee parcel, the state will have a stronger argument that under the balancing test, state interests outweigh tribal and federal interests, and therefore state taxation of sales to non-Indian customers should not be preempted.

Of course, whether the state would prevail in such an argument depends on the fact-specific and unpredictable application of the balancing test. But the tribe must decide whether to risk locating its business where the state will have a better likelihood of prevailing and therefore a greater incentive to litigate the issue. More often than not, the tribe will select the trust parcel to avoid the expense and delay of litigation and the risk of a negative outcome. Worse, many tribes have insufficient Indian country land holdings and will defer economic development while awaiting federal approval to take land into trust—a process that may take years and involves additional uncertainty and expense.

It is no accident, then, that tribal governments tend to concentrate on goods that are taxed heavily off reservations. Their longstanding dependence on cigarette sales, more recent dependence on gasoline sales, and emerging interest in marijuana sales are examples of this.[23] While casino gaming—which faces high state-erected barriers to entry and taxes—allows them a somewhat diversified economy, overdependence on these few sectors continues to limit tribal economies.

III. The *De Facto* Case for Change

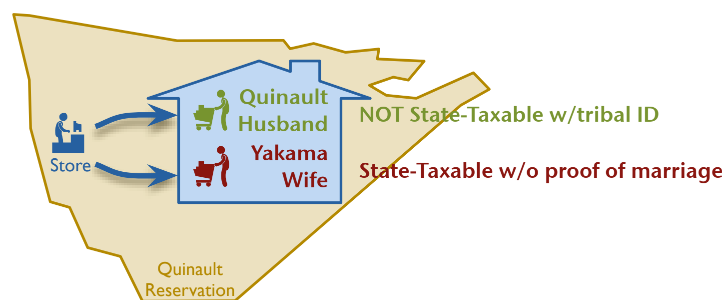
The precedents governing taxation on tribal lands may have made sense in their original context, but today they produce absurdities worthy of *Catch-22*. A few examples will make that clear.

Suppose a Quinault man and a Yakama woman marry and make a home on the Quinault Indian Reservation while retaining their Native citizenships (Figure 1). A business may sell goods and services to the husband in Quinault Indian country immune from Washington State taxation. However, because Washington can legally insist that the vendor collect and remit sales taxes from Yakama Indians living on Quinault but makes an exception in the case of marriage, the wife has to prove she is married to the Quinault member to enjoy the exemption. (WAC §458-20-192(5)) This not only puts a strange burden on the retailer—who must ask for proof of tribal affiliation *and* marital status at the register—but also intrudes into household decision-making. Does Mr. or Mrs. Underwood have the paperwork to do the Saturday shopping? (Washington law does not extend the exemption to children or other relatives of the couple.)

Figure 1

Citizenship-Based Taxation

Tax immunity may depend on tribal citizenship (and marital status)

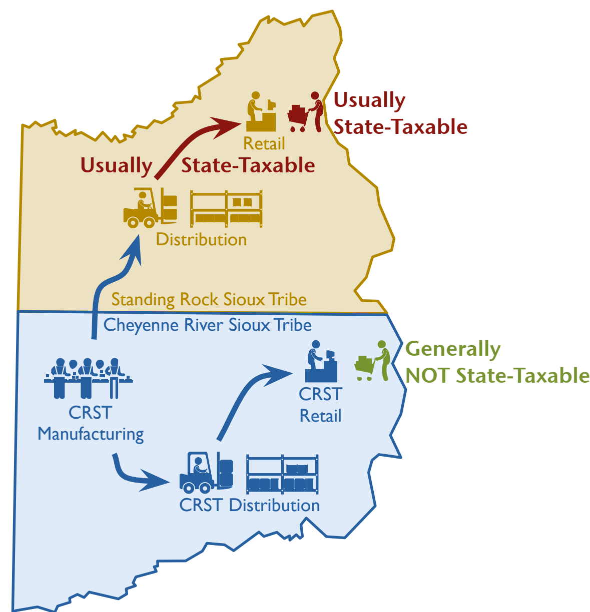


[23] "The main source of employment on reservations that do not enjoy the prosperity of gaming comes from the gas stations and cigarette shops that traditionally sell these products tax-free. This economic advantage helps tribes achieve self-sufficiency as sovereign nations. Most tribes are not blessed with oil reserves, or thousands of acres of timber (should they be willing to cut it down), providing a sound economic base. Most tribes, in fact, were given the poorest land or such a small parcel that any attempt at self-sufficiency would be very difficult. This difficulty was acknowledged when reservations were created." (Lazore, 1997)

Even more complexity arises if, instead of a household, the question involves an Indian-owned entity doing business on the Quinault Reservation. Under Washington law, if the business is incorporated and is "comprised solely" of members of one tribe, the corporation will be exempt from state tax on business conducted in that tribe's Indian country (and on treaty fishery activity conducted outside Indian country). Partnerships or other entities "comprised solely" of enrolled members of a tribe are treated the same. However, if the company "includes a family member who is not a member of the tribe…together doing business on the…reservation, the business will be considered as satisfying the 'comprised solely' criteria if at least half of the owners are enrolled members of the tribe" (WAC §458-20-192(5)(d)). So if a Quinault husband and his Yakama wife form a partnership, their business may make tax-exempt purchases in the Indian country of either tribe. But if their Yakama daughter joins the partnership, the tax exemption is lost at Quinault. If retailers and distributors are not willing to navigate these complexities, the business owners may have to pay the state tax and seek a refund later, which could be detrimental to their cash flow. Despite the complexity of this rule, Washington offers more clarity than states that have not set forth any guidance on the tax treatment of business entities owned, in whole or in part, by Indians.

As noted above, under the *Bracker* analysis, if an Indian country–based tribal business provides a service or adds value to a product, the sale of that service or good may be immune from state taxation in that tribe's Indian country if the balance of interests favors the tribe. Suppose a Cheyenne River Sioux metalworking facility turned sheet steel into waterproof metal boxes suitable for first aid kits or ammunition (Figure 2). Those boxes could be sold through a distributor or retailer on the Cheyenne River Reservation *to non-Indians* immune from state taxation if the distributor or retailer were also owned by Cheyenne River members or by the tribe. But if the same product were sold in any other tribe's Indian country, including the adjacent Standing Rock Sioux Reservation, the state could insist on taxing sales to non-Indians.

Figure 2
Place-Based Taxation
Value added by an Indian company is immune from state taxation in some places but not others



These absurdities arise from historical contingencies, but fiscal myopia explains, at least in part, how they maintain their force today. Two uncontroversial propositions should make clear why they must be eliminated:

1. Tribes that provide tax-funded essential public goods and invest in their businesses encourage economic growth.
2. As reservation economies grow, so do state economies and state tax collections.

Nonetheless, when states assert tax authority, policymakers tend to think in zero-sum terms—that is, they cannot imagine that state economies might benefit from giving ground on the primacy of state taxes. This view is shortsighted for several reasons.

Indian Economic Development Helps State Growth

Tribal economic development adds directly to gross state product when it brings underutilized resources into production; tribal land, infrastructure, natural resources, and other physical capital are put to higher and better use. Two examples are the Tulalip Tribes' replacement of a defunct Boeing facility at Quil Ceda Village and the invigoration of the Gila River Indian Community industrial park south of Phoenix. In far too many places around Indian country, physical capital goes underutilized. This is not merely a feature of remoteness (though that plays a part); it is often a consequence of the uncertainties and absurdities of the rules governing Indian economic development.

More important, *human* resources are better engaged when economic growth improves. From 2008 to 2012, the unemployment rate among Indians on Washington reservations averaged 20%. Such rates would indicate economic calamity if they occurred on a nationwide or statewide scale. Washington State averaged 8.8% in the same period. The unemployment rate does not count discouraged workers (those who have given up seeking work), so it pays to look at other measures, such as the labor force participation rate. In Washington, labor force participation on the reservations is 53%, as opposed to 66% statewide (US Census, 2014). Nationwide from 2006 to 2010, the picture was no better: Unemployment among Indians living on reservations in the lower forty-eight states was also more than twice the all-races rate (Akee & Taylor, 2014).[24] Addressing this issue is a high priority for tribal governments. It should be for the states, too. After all, Indians are also state citizens.

When an unemployed worker gets a job, the gains for gross state product can be large. Not only is that worker productively engaged in the economy (personal income is the lion's share of gross national product), but he or she is no longer dependent on family members, taxpayers, or both. Thus the swing in GSP may be substantially larger than just the salary benefit, depending on the situation.

In addition, when tribal government spending addresses social, educational, housing, environmental, and health deficits, it benefits a state's economy. Of course, there is a direct effect on the state treasury when, for example, a tribal social worker spends her paycheck on groceries and electricity. Given that Indian country economies are predominantly small, undiversified, and remote, virtually all their households and businesses turn to the off-reservation economy for goods and services.

More important, when the social deficits themselves are addressed, the state economy benefits. Take education. The McKinsey Global Institute (2009a) estimates that addressing the racial gap in US education would raise national GDP from 2.2% to 3.7%. "These educational gaps impose on the United States the economic equivalent of a permanent national recession" (McKinsey and Company, 2009b, p. 5).[25] Black and Latino test scores (not Indian scores) determine McKinsey's "racial gap" in accordance with those groups' larger numbers, but comparable test scores for Indian schoolchildren were at the low end of those groups' (National Center for Education Statistics, 2012), making the per capita impact of closing the Indian education gap even larger.

And so it goes with early childhood education, drug rehabilitation, college scholarships, diabetes prevention, financial literacy training, and myriad other tribal social investments: State economies benefit when Indians participate more in the state economy and are better educated, healthier, and more secure. What governor would seek to create pockets of *limited* human capital within state borders?

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[24] Recent rates of reservation unemployment for all but the largest reservations are available only in the Census Bureau's American Community Survey (ACS) five-year averages. For strict comparability, the statewide (and nationwide) all-races ACS five-year averages are also used.

[25] See also Auguste, Hancock, and Laboissière (2009).

States commonly oppose tribes' sovereignty and the economic activity generated by that sovereignty on the ground that successful business and employment creation *reduces* business incomes and employment in surrounding non-tribal areas. Nowhere are such claims more frequent than in the case of tribal casinos. Astoundingly, some critics of tribal economic sovereignty argue that Indian casinos have a recessionary impact (Anderson, Cotton & Watkins, 2003). Somewhat more reasonable critics claim that state revenue collection drops when Indian economic development takes off (Anders, Siegel & Yacoub, 1998; Washington Research Council, 2002).

Implicitly or explicitly, the thinking behind these claims is that when Jane and her friends visit the Puyallup Tribe's Emerald Queen Casino for a steak dinner, a Jay Leno show, and an hour or two at the slots, they are not at the local—and state-taxed—P.F. Chang's, AMC Theater, and Cold Stone Creamery. Appealing as the story may be, the conclusion that Indian economic growth causes state fiscal shrinkage goes begging for persuasive empirical support (Taylor, 2005 pp. 33–38).

And for good reason: No reservation economy can provide all the carpeting, electricity, poker chips, asphalt, computers, and police cruisers that tribal governments and businesses require. They have to turn to the off-reservation economy. In Washington State, two-thirds of all tribal employees are non-Indians—18,000 out of 27,000 in 2010 (Taylor, 2012a). In addition, Washington tribes buy the vast preponderance—more than 94%—of their goods and services from off-reservation suppliers (Taylor, 2006). This heavy reliance on off-reservation resources—widespread in Indian country—explains why claims of economic harm from Indian economic development should be met with skepticism. Non-Indian workers and suppliers pay property and sales taxes in Washington and other states (and income taxes, too, in the states that levy them).

The evidence that reservation economic growth benefits state economies is accumulating. Tribal leaders know this firsthand. An off-reservation RV repair shop owner in Shelton, Washington, told Squaxin Island tribal leaders that business boomed after the tribe opened its nearby Little Creek RV Park. Business leaders in Payson, Arizona, shared their relief that the Tonto Apache Tribe's Mazatzal Casino became one of the largest employers in town just as its sawmill was shutting down (Taylor, Grant, Jorgensen & Krepps, 1999). A local chamber of commerce reported:

> The single largest contributing factor to economic success has been the Mill Bay Casino [on the Colville Reservation]. Their aggressive marketing stance has drawn visitors by the busload to our hotels, boosting occupancy during a time period which traditionally has meant employee layoffs....They are the single largest private business employer in the region, pumping payroll dollars into every facet of our community through direct purchases, indirect purchases, payroll taxes, school taxes, sales taxes and more. (Lake Chelan Chamber of Commerce, 1996, p. 402)

More recently, a coalition of six towns, five chambers of commerce, a county, and seven other off-reservation government agencies and private associations observed in an amicus brief to the US Supreme Court that:

> The [Match-E-Be-Nash-She-Wish] Band's economic development efforts on the trust lands have directly created 900 new jobs and infused area hotels, restaurants, and other businesses with much-needed customers and revenues....The Band's economic development efforts have facilitated intergovernmental service-sharing agreements that are critical to the region's recovery. (Wayland Township, 2012, p. 5)

These observations reflect the destination effects and regional multiplier impacts that Indian economic activity produces for the off-reservation economy—including in *non-Indian* employment and *state* tax collection. Direct, indirect, and induced impacts[26] on gross regional product, employment, and tax collection have been variously documented in studies of tribal colleges (Coon, Bangsund & Hodur, 2013; Diaz & Pina, 2013), tribal timber operations (Clements & Marcouiller, 2008; Kalt, 1993), tribal procurement businesses (Taylor, 2012b), and tribal casinos (Carstensen et al., 2000; Ha & Ulmer, 2007; S. Peterson, 2010; Thornberg, Levine, Shepard & Meux, 2012).[27]

Impact model estimates are confirmed by before-after and adjacent-remote data on economic activity. For example, according to the Thurston County tax assessor's records (2009), when the Great Wolf Lodge opened, privately owned, off-reservation properties within a mile experienced an average of 14% growth in value, while parcels in the county as a whole appreciated by only 4% (as cited in Kalt, 2009). Broad statistical and econometric analyses show employment gains in nearby counties when an Indian casino opens (Baxandall & Sacerdote, 2005; Baxandall, O'Brien & Sacerdote, 2005; Evans & Topoleski, 2002; Taylor, Krepps & Wang, 2000) and income gains in California census tracts near Indian casinos (Akee, Spilde & Taylor, 2014; Martin et al., 2006). The economics, anecdotes, models, data, and econometrics corroborate one another: Reservation economic growth begets nearby economic growth.

Double Taxation Is a Double Bind

In view of the benefits to the state of Indian economic development, the burden of double taxation appears particularly counterproductive. When states and counties insist on applying their tax powers in Indian country, a tribe adds to the residents' tax burden if it institutes its own

[26] "*Direct effects*…[are] the impacts (e.g., change in employment) for the expenditures and/or production values specified as direct final demand changes [of a given project or economic activity]; *indirect effects*…[are] the impacts (e.g., change in employment) caused by the iteration of industries purchasing from industries resulting from direct final demand changes; *induced effects*…[are] the impacts (e.g., change in employment) on all local industries caused by the expenditures of new household income generated by the direct and indirect effects of direct final demand changes." (Minnesota IMPLAN Group, 2004, p. 81)

[27] See also the annotated bibliography compiled by Gardner, Spilde, & Kalt (2005) and more recent work by one of us (Taylor, 2005; 2006; 2008; 2009; 2012a; 2015).

tax. Companies, behaving rationally, flee Indian country. The US Government Accountability Office has noted, for example, that:

> [d]ual taxation of resources does not occur on private, state, and federally owned resources and can make development less economically attractive and discourage development of Indian resources. (2015, pp. 29–30)

States and counties make no meaningful effort to spur reservation economic development, so tribes must do it themselves—ironically without the ability to tax the very activities that enable the tribe to underwrite its creation.

Double taxation puts tribal governments in a double bind: Levy a tax to recover investments in development and cause businesses to flee, or do not levy a tax and fail to recover the costs of investing in development. The consequence is that most tribes have a very limited commercial tax base (Fletcher, 2004). Generally, they turn to government-owned-enterprise profits, lease revenue, and natural resource sales for revenue—sources tapped minimally by all but the most resource-rich states (e.g., Alaska)—because tribal members have few taxable resources or activities for their governments to tax. The rest of the world is privatizing, and for good reason (Megginson & Netter, 2001), but the share of Indian country GDP that is owned by tribal governments is burgeoning, dominated by casinos and resource industries. To paraphrase the complaint of at least one tribal CEO, federal law forces tribes to be socialist in the ownership of production.

Quil Ceda Village, a federally chartered municipality on the Tulalip Indian Reservation, demonstrates the challenge presented by a state's insistence on the primacy of its own sales tax. Before the Tulalip Tribes developed the village, the corridor west of Interstate 5 on the east end of the reservation contained little more than vacant land and an abandoned industrial building, once leased to Boeing. To spur development, the Tribes replanned the area, created a governing board, chartered the municipality under federal law, and built infrastructure—the roads, water lines, water treatment facility, telecom lines, and other capital necessary to recruit and retain tenants. It then leased space to companies ranging from Cabela's and Home Depot to Walmart and Seattle Premium Outlets.

As a landlord, the Tulalip Tribes earn lease revenue from tenants commensurate with the Tribes' position in the marketplace for commercial real estate. As a government, however, Tulalip cannot reap what it has sown, because the state's insistence on collecting various taxes at the shops in Quil Ceda Village precludes the tribal government from imposing its own tax. The village produces millions for the state. It yielded an estimated $26 million in sales and use taxes in 2005 (Taylor, 2006). By 2013 that figure was $37 million, with an additional $2.1 million in business and occupation taxes (*Tulalip v. Smith* (Compl.), 2015, pp. 18–19; *Tulalip v. Smith* (Smith Answ.), 2015, pp. 9–10). The state also collects personal property and other taxes at Quil Ceda. Yet the government that created, maintains, polices, and supports the village has received none of these tax receipts. The vacant land and the Boeing facility were once wasting assets; now more than 1,000 people go to work at Quil Ceda, and tens of thousands visit there. All around Indian country, idle land provokes the question, What economic benefits would emerge if

uncertainty and intransigence did not prevent tribes from reaping the tax revenues from whatever investments they might make in public goods and infrastructure? The answer is plain: If states allowed tribal governments to reap tax revenue where they sowed economic infrastructure, reservation *and* state economies would grow.

Much of the foregoing discussion might be moot if states provided infrastructure, public goods, and services on reservations in proportion to tribal needs. But generally they spend less on reservations than elsewhere, choosing to defer to the federal and tribal governments. This practice runs against the grain of intrastate financing rules that cause all or the vast majority of certain taxes to flow back to the jurisdictions that generate them. State sales tax revenue, for example, may be generated on the reservations, but it flows back to state and local governments.

The Mandan, Hidatsa, and Arikara Nation in North Dakota is experiencing an extreme version of this phenomenon. Development of the Bakken formation in and around its Fort Berthold Reservation has been aggressive, putting the region on par with Texas and Alaska in fossil fuel production. The hundreds of millions of dollars that North Dakota has collected from the reservation in recent years have helped to create a $3.3 billion state surplus fund (Murphy, 2015). Meanwhile, according to Secretary of the Interior Ken Salazar, development of the formation has damaged reservation roads and increased traffic accidents and crime (2013). The tribes observe that in 2011 alone, North Dakota collected $82 million in taxes from energy development but spent less than $2 million on state roads and zero on tribal and BIA roads (Mandan, Hidatsa, and Arikara Nations, 2015). The production companies themselves are undertaking road maintenance, an arrangement they recognize as unsustainable as they ask the elected leadership of North Dakota to recognize "the growing need for additional funding for Fort Berthold and the people of the MHA Nation" so that they can address "the impacts that come with rapid growth, including housing shortages, inadequate emergency, health and social services, and growing maintenance needs for roads and infrastructure" (Ness, 2013). As the president of the North Dakota Petroleum Council, Ron Ness, further notes on their behalf:

> There is an incredible opportunity resulting from oil and gas production for all North Dakota citizens, including those living on Fort Berthold. The availability of increased funding will help the MHA Nation *meet their infrastructure needs*, will provide *benefits to the surrounding communities* and provide important assurance that North Dakota continues to be a state that provides *opportunity and fair treatment for all its citizens*. (2013, emphasis added)

Private enterprise sees and bears the consequences of ambiguity in Indian tax policy, and the disincentives of double taxation for natural resource development can create net losses for the economy, particularly where the resources in question are close to the margin.[28]

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[28] As Alexander (1997) points out, state taxation power over Indian natural resources introduces the risk that taxes on resource rents will exceed nondistortionary levels and thereby introduce deadweight losses in contexts that would not otherwise suffer them. This risk may be small for infra-marginal resources such as the Bakken, but it is

Tax Breaks versus Broken Taxes

While the states insist on asserting tax jurisdiction over Indian country, to the detriment of Indians and non-Indians, they give tax breaks to myriad other groups. A 2012 Washington State Tax Exemption Study identified 452 state and local tax exemptions worth $29.3 billion over the 2011–2013 biennium. By its accounting, some exemptions eclipsed actual collections: Business and occupancy exemptions ($7.7 billion) were 117% of the $6.5 billion collected. The retail sales and use tax exemptions in that biennium amounted to 45% of the total potential tax base (Washington State Department of Revenue, 2012a, pp. 2–4).

Certain taxes are outside the legislature's reach and must be exempted, including those that would discriminate against or excessively burden interstate commerce, so Washington law specifically exempted $2.2 billion in that biennium. Some state tax exemptions exist because otherwise money would move from one governmental pocket to another—though when it comes to taxing tribal governments or the individuals and businesses to whom they provide services, this principle is rarely recognized and the resulting exemptions are fairly tortured.[29] Other exemptions recognize impracticalities such as apportioning tax liability for stocks and bonds or other intangible property. Should the taxpayer be the business or the shareholder? Easier just to exempt the property (Washington State Department of Revenue, 2012a, pp. 6, 8).

Nonetheless, the preponderance of exemptions—up to 91%—result from policy choices the legislature has made or could undo. Among their many purposes are: recruiting businesses to the state, sheltering low-income consumers, aiding farmers, and assisting nonprofit hospitals (Washington State Department of Revenue, 2012a, pp. 5–7). These forgone taxes can be quite large: Though Washington does tax some services, it did not collect $4.8 billion in sales taxes on "personal and professional services" in the biennium—equivalent to more than a quarter of all sales and use tax exemptions (Washington State Department of Revenue, 2012b). We have neither the scope nor the space here to weigh the merits of Washington's many exemptions. Suffice it to say that tax breaks are a regular and and large feature of state fiscal policy.[30]

Against this backdrop, the state's insistence on tax jurisdiction in Indian country appears particularly closefisted—especially absent any evidence that its tax policies are spurring reservation economic growth. A back-of-the-envelope calculation puts this into perspective: If

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likely to burden the very timber, oil, coal, and gas that it should not—the resources in Indian country that have the thinnest margins.

[29] For example, a Washington State property tax exemption for tribal fee lands used for essential governmental purposes makes clear that commercial activities on recently acquired lands are excluded in the definition (RCW 84.36.010), although revenue from those activities may support essential government functions precisely because the tribe lacks an adequate tribal tax base.

[30] Interestingly, one argument frequently offered by state and local officials for a refusal or reluctance to retrocede from state taxation in Indian country is a fear that tribes will not impose taxes, or will impose taxes at lower rates, and thereby encourage businesses to locate in Indian country. Although this practice is standard and well accepted among nations, states, and local governments, some state and local officials (and judges) apparently believe that tribal sovereigns should not be permitted to use it to develop their economies.

every one of the 29 federally recognized tribes in the state were to develop a Quil Ceda Village as successful as the original, *and* Washington were to forgo the sales tax revenues therein, *and* there were no accompanying impetus to growth statewide (contra economics), the annual tax "break" would amount to about 2% of Washington's annual exemptions in the 2003–2005 biennium (Welch, 2004).[31]

These are herculean ifs. Few tribes could generate the sales made possible by Tulalip's proximity to I-5 and the state's largest population center. What's more, growth on the reservations would indeed drive growth in the state-taxable economy, raising revenue—these successful Quil Ceda Villages would create thousands of jobs that produced their own benefits to the state treasury. And Washington's tax concession to tribes need not mean a tax *disappearance*—tribal governments can and do mimic state tax rates, whether compacted to or not. In other words, 2% greatly overstates the forgone *government* revenue statewide.

Thus, Washington is in effect saying, We're willing to spur economic growth and aid groups we care about by forgoing taxes completely, so long as Indians aren't involved.

How is that justifiable?

Consider, in contrast, Nevada's position on sales tax in Indian country. By law, Nevada does not collect tax on sales of tangible personal property in Indian country if: i) the tribal tax is equal to or greater than the tax imposed under state law; and ii) a copy of an approved tribal tax ordinance imposing the tax has been filed with the state Department of Taxation (NRS 372.805). Since the adoption of this provision, in 1989, the Reno-Sparks Indian Colony has diversified its economy from "sole reliance on tobacco revenues" and now leases and develops commercial sites to support tribal government functions. Tenants include Walmart, a Mercedes Benz dealership, and locally owned and operated businesses. The availability of a tax base has allowed the Tribe to contribute to the region's infrastructure, often in partnership with nearby governments and companies, and to provide services to Indian and non-Indian citizens by installing traffic signals, building levees, operating a health clinic open to non-member Indians, and performing environmental cleanup (Reno-Sparks Indian Colony, 2015). Fitch Ratings upgraded the Tribe's long-term issuer default rating to BB+ from BB in 2013, noting that "The upgrade reflects important strides in diversifying away from declining tobacco related sales tax revenues" but that tribal "revenues remain concentrated and heavily dependent on economically sensitive sales and excise taxes" (Meyer, 2013).

Other states have ceased collecting the full amount of state taxes in Indian country under compacts and other agreements with individual tribes. Although numerous such agreements exist, they address just a small fraction of the issues resulting from concurrent tax jurisdiction. State-tribal tax agreements tend to be negotiated only when the tribe has strong legal leverage and/or the state has enforcement limitations. They also generally have expiration dates, putting their renewal at risk in subsequent election cycles, and states are often able to insist on tax

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[31] The older biennium is used here for macroeconomic comparability to the available data from the Department of Revenue for Quil Ceda Village collections. The percentage estimated here would vary over time, of course.

parity and/or revenue-sharing provisions that restrict the tribe's ability to attract economic development and establish a sufficient tax base.

Although these agreements are an exceptionally successful model for some tribes and states, they are far from a complete solution to the problem. Tiebout competition between governments (see note 13) implies that a given tribe's economic, demographic, and resource context ought to be reflected in its tax strategy. The implication of the Reno-Sparks story and other successful negotiated solutions is that resolving the double bind can be powerful. Certainty about apportionment can bring economic vibrancy that benefits tribes *and* states, even in the absence of tribal rate advantages or when resolved fully in the tribe's favor.

IV. The *De Recto* Case for Change

The preceding sections made *de jure* and *de facto* arguments for reforming state approaches to taxation in Indian country: The law is a mess and hobbles economic development. There is also a principled moral case to be made, one based on just claims.

Indian Priority

The sovereign status of tribes, and their relationship to the federal government as nations predating the formation of the United States, has been consistently affirmed by the Supreme Court. In 1832, the Court made clear that this tribal-federal relationship preempted interference by the states:

The Cherokee nation, then, 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 assent of the Cherokees themselves, or in conformity with treaties and with the acts of Congress. The whole intercourse between the United States and this nation is, by our Constitution and laws, vested in the Government of the United States. (*Worcester v. Georgia*, 1832, p. 520)

In the absence of congressional authorization, state regulatory incursions in Indian country, and the court decisions that allow them, violate the very essence of the nation-to-nation relationship established between tribes and the federal government.

If tribes preexist the United States, ought not first-in-time tribal governments be first in the right to tax, too? As the Supreme Court noted of the Treaty with the Yakama of 1855, "[T]he treaty was not a grant of rights to the Indians, but a grant of rights from them—a reservation of those not granted" (*US v. Winans*, 1905, p. 381). If the tribal power to tax has not been extinguished, how is it that tribal governments should be second in line to tax? Do we give the second homesteader the water rights of the first? Of course not. And unlike water rights, sound tax policy is not about dividing scarce natural resources but, rather, about underwriting the economically beneficial production of public goods with positive spillovers such as infrastructure and community health—in this instance for reservations that desperately need both.

Fair Dealing

Tribes are constitutive sovereigns of the United States. As Kalt & Singer observe:

> Indian nations were the original sovereigns and owners of the land now occupied by the United States....The United States was not formed merely by the Constitution, but by the treaties entered into with Indian nations. Those treaties form the original framework of American government and recognize both tribes' sovereignty and retained property rights. (2004, p. 15)

Indian land cessions gave the governments of the United States their geographic and political fields of action. Washington can tax economic activity in Seattle today because the Duwamish, Suquamish, Snoqualmie, Snohomish, Skagit, Swinomish, and others ceded the territory for it at Muckl-te-oh in 1855. At the same time, the tribes retained land and rights. (*Treaty of Point Elliott*, 1855, 2014)

Yet by a tortuous legal and political path, Washington tribes have arrived today at a state of affairs where:

1. The state taxes Indians and non-Indians on lands ceded by Indians
2. and insists on taxing non-Indians on lands Indians did not cede,
3. rendering tribes effectively unable to tax on their own lands,
4. though the tribes bear governing responsibilities to Indians *and* non-Indians within those lands,
5. and the state abdicates its responsibilities there,
6. forcing reservation economic activity to rush into tribal government ownership, adopt contractual contortions, or languish altogether.

To believe that Indian treaty signatories intended to create this mess violates the logic of fair dealing. Think about it federally: Would we give Massachusetts the right to tax its citizens' purchases *at the cash registers* of sales-tax-free New Hampshire (as Washington insists on taxing sales within Tulalip-created Quil Ceda Village) or, for that matter, their leasehold interests in a Florida timeshare? Probably not.

More to the point, even if so, would we simultaneously *not* give New Hampshire or Florida the reciprocal right to tax its citizens within Massachusetts? Absolutely not. But that is how double taxation works for Indian tribes. As reasonable as every precedential step along the way may have seemed, Indian tax law today is a heads-states-win, tails-tribes-lose proposition. No tribe could conceivably have agreed to it. It was compelled. It was imposed.

Modern Supreme Court cases giving states the power to harm tribes not only burden reservation economies but contradict long-standing congressional and executive branch policies respecting tribal sovereignty, advancing Indian self-determination, and embracing government-

to-government relationships.[32] Indian tax law is incongruous with current policy, though the policy is credited with partial recovery in Indian country:

> Since the 1970s, federal American Indian policy in the United States has been aimed at promoting self-determination through self-governance by federally-recognized tribes. This policy has proven to be the only policy that has worked to make significant progress in reversing otherwise distressed social, cultural, and economic conditions in Native communities. (Cornell & Kalt, 2010, p. v)[33]

Don't Beggar Your Neighbor

In principal part, tribes lack significant tax revenue not because their power to tax has been nullified but because Washington and other states insist on asserting tax jurisdiction in Indian country. When tribes cannot preempt that jurisdiction, they are relegated to second-class status. When states inflict on them the Hobson's choice of double-taxing economic activity or not taxing at all, they beggar their neighbors, to use Adam Smith's phrase; they ease their own fiscal burdens by worsening the tribes'.[34]

The law may allow this, but *de jure* might does not make *de recto* right. To the contrary, insisting on state tax primacy forces a continuing transfer from Indians to states. Tribes may build infrastructure to recruit businesses, as at Quil Ceda, but unless the state relents, they don't dare add a second tax. Meanwhile, states reap revenue where they did not sow.

And that is the benign story. Tribes refrain from investing in public goods and services when legal uncertainty makes cost recovery through tax collection doubtful or entirely out of reach. Thus, they leave vacant land vacant and empty buildings empty, and reservation poverty grinds on. State policymakers who are comfortable with the moral implications of not relenting on state tax primacy may want to think again. How is this not an ongoing, modern-day expropriation from Indians?

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[32] As advanced, for example, by executive orders and pronouncements (G. H. W. Bush, 1991; G. W. Bush, 2004; Carter, 1979; Clinton, 1994, 2000; Nixon, 1970; Obama, 2009; Reagan, 1983); by tribal "treatment as state status" in the Clean Air Act (45 USC §7601(d)(1)(A)) and Clean Water Act (42 U.S.C. § 300j–11); and by many statutes that encourage tribal authority, discretion, and control, such as the Indian Self-Determination and Educational Assistance Act of 1975 (PL 93-638) and the Native American Housing Assistance and Self-Determination Act of 1996 (PL 104-330).

[33] See also The state of the Native nations: conditions under US policies of self-determination by the Harvard Project on American Indian Economic Development (2008).

[34] "[N]ations have been taught that their interest consisted in beggaring all their neighbours. Each nation has been made to look with an invidious eye upon the prosperity of all the nations with which it trades, and to consider their gain as its own loss. Commerce, which ought naturally to be, among nations as among individuals, a bond of union and friendship, has become the most fertile source of discord and animosity." (Smith & Cannan, 2003, p. 621)

The centuries-long history of state and federal policies aimed at (or having the effect of) capitalizing the US economy with tribal assets has been injury enough.[35] In light of abundant contemporary evidence showing that tribal management of tribal assets benefits both on- and off-reservation economies,[36] state tax primacy in Indian country appears particularly anachronistic.

Parity in Breaks

As noted above, Washington exempts taxes worth billions of dollars for many reasons, not least of which is economic development. The state has refrained from fully taxing Boeing, lawyers, farmers, and many others. Yet it cannot seem to do right by tribes on this front (not to mention act in its own economic interest) unless compelled to do so. Other states are similar. Why should states be less eager to champion policies that foster economic development in Indian country than they are to spur and support economic development in rural areas and depressed counties or to attract and retain multinational firms?

V. Recommendations

Although tax policy is never settled, the fundamental principles of good tax policy and the practical and economic benefits of intergovernmental accommodation have changed little over centuries. Federal, state, and local governments share the goals of certainty, economic growth and efficiency, and reliability of revenues, and have found ways to arrive at reasonably fair apportionment. Unfortunately, tribes have usually been overlooked or exploited in this process. They operate under a complex set of legal precedents that skew, delay, and often prevent economic development in Indian country, damaging the ability of tribal governments to fund essential functions. The loss of economic activity and job creation is harmful to all governments and citizens, tribal and non-tribal.

Much of the case law in this area, and the attitudes that policymakers bring to these issues, are based on precedents and ideas formed long before tribes developed modern economies and had the financial resources to begin providing significant governmental programs and services. The law and the policy are shot through with the false presumption that state or local governments are providing significant benefits in Indian country while the tribes are merely “marketing tax advantages,” as in the opinion of the US Supreme Court that:

> Washington’s taxes are reasonably designed to prevent the Tribes from marketing their tax exemption to nonmembers who do not receive significant tribal services

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[35] For example, Wilkinson reports that Indian landholdings fell from 138 million acres in 1887 to 52 million in 1934 (i.e., well after the treaty-making period) under the terms of the Dawes Act (1987, p. 20), legislation that was apparently supported by well-meaning reformers, not just opportunists seeking land (Carlson, 1981).

[36] For example, Krepps and Caves (1994) show that by resolving principal-agent slippage, tribal management of tribal forests produces more harvesting of the sustainable yield and higher prices for commodity lumber, all else being equal.

> and who would otherwise purchase their cigarettes outside the reservations. (*Washington v. Colville*, 1980, p. 157)

But state and local governments have long marketed tax advantages to attract and retain business. For example, per the New Hampshire Department of Resources and Economic Development:

> It's time to get real—in New Hampshire—where shopping is infinitely more blissful to do than to imagine. After all, even that big online retailer will charge you sales tax these days, but here in New Hampshire, we still say "no" to taxing purchases (2015).[37]

This Web-based marketing is apparently addressed even to out-of-state visitors "who do not receive significant [New Hampshire] services and who would otherwise purchase their [retail goods] outside the [state]," to adapt *Colville*'s language to an interstate context.

This view is antiquated when most tribes provide the same infrastructure and services that their neighboring non-tribal jurisdictions do (if not more). In this context, the convention that each government shall tax what goes on in its jurisdiction makes more sense.

The place of tribal governments in our collective and interdependent economy must be reassessed if good tax policy is to be achieved. Just as federal, state, and local governments ignore the impact of the global economy at their peril, a failure to recognize that their tribal neighbors activate economic resources and provide essential governmental programs and services is self-destructive.

But how can tax policy be repaired in an arena with so many deep and historical flaws?

Federal Solutions

Resolving Indian tax issues on a state-by-state basis has had mixed results, takes a long time, and has very different outcomes depending on political and economic goals and the leverage of the parties, exacerbating the tendency to litigate. Congress and the Bureau of Indian Affairs could significantly reduce uncertainty and conflict.

Congress could eliminate state and local government taxation in Indian country that is based on the citizenship status of businesses and customers. Tribes could be afforded the same comprehensive and exclusive tax authority that states now have in their geographic jurisdictions. Such legislation would have a significant economic impact on state and tribal governments, and might entail the transfer of responsibility for some governmental functions. A phase-in period

[37] Or Travel Portland: "In Portland, [Oregon,] you'll find everything you expect from big-city shopping—except the sales tax. Pick up everything in Portland (everything!) without sales tax. From handmade items to designer goods, you'll find it all, tax-free" (2015). And the Anchorage (Alaska) Convention and Visitors Bureau touts "no sales tax" (n.d.).

would ensure a smooth transition and allow states and tribes to negotiate agreements where appropriate on issues such as tax administration and provision of services.

Intermediate and piecemeal solutions are also possible. Congress could, for example, create an exemption from state tax where a substantially equivalent tribal tax is imposed, thereby eliminating the specter of dual taxation that creates uncertainty for tribes and non-Indian investors alike. Congress could also act with regard to any specific subset of state taxes, such as sales or excise taxes; could permanently extend tax credits available to employers in Indian country; and could broaden the availability of tax-exempt bond financing in Indian country by giving tribes the same latitude that state and local governments have to finance projects such as golf courses and conference centers. The more piecemeal the approach, the less likely that good tax policy would be achieved. But in a system so broken, a staged approach would be better than the status quo.

The Bureau of Indian Affairs could increase certainty within existing law through a comprehensive update of the Indian Trader regulations at 25 C.F.R §140. These regulations, which have not been updated since 1957, utterly fail to address the needs of Indian country today and impose an unnecessary burden on tribal economic development. And, as the National Congress of American Indians has observed,

> The underlying law at 25 USC §262 is broad and flexible authority for the Department of Interior to adopt new regulations that would meet the economic development and tax revenue needs of Indian tribal governments in the 21st Century. (2015, p. 1)

Just as the BIA (2012, 2016) clarified tax treatment of activities occurring on leased Indian lands with regulations that became effective in January 2013, and of rights-of-way on Indian land with regulations that became effective in March 2016, the agency could through Indian Trader regulations provide comprehensive analysis and guidance on tax related to all business activities in Indian country. Similarly, the Internal Revenue Service could provide modern interpretations of existing statutes.

State Solutions

In the absence of federal legislation or regulation, states have tremendous opportunity to resolve Indian tax issues in ways that address unique local circumstances and benefit all citizens of the state. All that is lacking in many cases is acceptance of the well-established fact that encouraging tribal economic development through good tax policy helps state and local economies. So long as state officials and the public incorrectly believe that strengthening the tribal tax base will hurt state or local economies, it will be impossible to muster the political will to engage in productive negotiations and legislation.

Like Congress, states could eliminate state and local taxes in Indian country that are based on the citizenship status of businesses and customers. Again, a phase-in period would allow for agreements to be negotiated where appropriate.

Intergovernmental agreements and statutory exemptions on sales, cigarette, fuel, timber, property, and other taxes in Indian country have proven beneficial for both tribal and state governments around the country.[38] For example, in Washington, tribes and the state worked together to secure legislative authority for cigarette tax compacts in 2001 (RCW 43.06.450),[39] timber tax compacts in 2007 (RCW 43.06.475), fuel tax compacts in 1995 and 2007 (RCW 82.36.450), and marijuana compacts in 2015 (RCW 43.06.490). These compacts are widely acknowledged to have resolved decades of costly litigation (see, e.g., Washington State Department of Licensing, 2013) and generate revenues critical to the provision of essential tribal government services, including transportation infrastructure used by Indians and non-Indians.[40] Washington also adopted a statutory property tax exemption for "all property belonging exclusively to any federally recognized Indian tribe, if (a) the tribe is located in the state, and (b) the property is used exclusively for essential government services" (RCW 84.36.010). The legislature said:

It is the legislature's specific public policy objective to create jobs and improve the economic health of tribal communities. It is the legislature's intent to exempt property used by federally recognized Indian tribes for economic development purposes, in order to achieve these policy objectives. (RCW 84.36.010; 2014 c 207 § 5)

Not only do these mechanisms provide certainty that supports increased economic development and attendant job creation, but they reduce conflict and help create an environment in which state and tribal governments can work together productively to resolve

[38] For example, in Washington State: "The legislature finds that these cigarette tax contracts will provide a means to promote economic development, provide needed revenues for tribal governments and Indian persons, and enhance enforcement of the state's cigarette tax law, ultimately saving the state money and reducing conflict." (RCW 43.06.450); "The legislature finds that in certain areas of taxation, where both a tribe and the state have jurisdiction and where there are challenges to administering a tax, tax agreements between the state and a tribe are a sound approach to resolving issues and simplifying processes. The legislature specifically recognizes that in the area of the timber excise tax, within the boundaries of the Quinault Reservation, the state faces challenges due to access to land and access to taxpayers. The activity being taxed takes place entirely within the reservation and is regulated by the tribe and by the state. The legislature therefore finds that shifting from a state administered tax, to a tribal tax credited against the state tax, will bring benefits such as consistent taxation, improved forest practices and water quality, improved fisheries, and sustainability. The legislature intends to further the government-to-government relationship between the state of Washington and the Quinault Nation by authorizing the governor to enter into an agreement related to timber harvest excise taxes." (RCW 43.06.475; 2007 c 69 § 1.); "The legislature finds that these agreements will facilitate and promote a cooperative and mutually beneficial relationship between the state and the tribes regarding matters relating to the legalization of marijuana, particularly in light of the fact that federal Indian law precludes the state from enforcing its civil regulatory laws in Indian country. Such cooperative agreements will enhance public health and safety, ensure a lawful and well-regulated marijuana market, encourage economic development, and provide fiscal benefits to both the tribes and the state." (RCW 42.06.485; 2015 c 207 § 1.)

[39] After adoption of this legislation, additional tribes opted in through legislation in 2002, 2003, 2005, 2007, and 2008 (RCW 43.06.460).

[40] See, e.g., Brief *Amicus Curiae* of Indian Tribal Governments Party to Fuel Tax Agreements (as Amended), *Automotive United Trades Association v. Washington, Jay Inslee, Pat Kohler*, Supreme Court of the State of Washington, No. 89734-4, pp. 4–5 (describing major contributions to transportation projects on state and county roads by the Puyallup, Tulalip, Jamestown S'Klallam, and Swinomish tribes).

other issues, including public safety, environmental protection, transportation, and infrastructure and services enjoyed by all citizens. Compact terms should be lengthy to strengthen that certainty.

Despite these successes, intergovernmental agreements and statutory exemptions remain relatively rare in comparison with the number of complex tax issues facing tribes today. States that have resolved some of these issues through laws and agreements should consider addressing others in similar ways. And states that have yet to do so should take note of success stories elsewhere in finding solutions that will work in their jurisdictions.

States could also achieve greater equity by promptly and properly implementing existing federal law and case law that recognizes tax exemptions in Indian country, such as the BIA leasing regulations adopted in 2012 and the underlying federal statutes, which exempt significant property and activities from state tax. Similarly, the 1980s smoke shop cases that allowed states to impose "minimal burdens" on tribes to collect state taxes from their non-Indian customers (*Department of Taxation and Finance of New York v. Milhelm Attea & Bros.*, 1994; *Moe v. Confederated Salish & Kootenai Tribes*, 1976; *Washington v. Colville*, 1980) should be reinterpreted in light of modern circumstances in which tribes are operating sophisticated businesses and not merely marketing a tax advantage. Rather than seeking to interpret such law as narrowly as possible to avoid losing even a single dollar of direct state or local tax, states should recognize the larger financial and social gains they will enjoy when barriers to economic development and the provision of governmental services are removed in Indian country.

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Native Nations Institute
803 E First St. | Tucson, AZ 85719
nni.arizona.edu

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Harvard Project on American Indian Economic Development
79 John F. Kennedy Street | Cambridge, MA 02138

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