08-55809

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

RINCON BAND OF LUISENO MISSION INDIANS OF THE RINCON RESERVATION, a/k/a RINCON SAN LUISENO BAND OF MISSION INDIANS a/k/a RINCON BAND OF LUISENO INDIANS,

Plaintiff-Appellee,

v.

ARNOLD SCHWARZENEGGER, Governor of California; STATE OF CALIFORNIA,

Defendants-Appellants.

On Appeal from the United States District Court
for the Southern District of California
No. 04-CV-1151 W (WMc)
William McCurine Jr., Judge

APPELLANTS' OPENING BRIEF

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INTRODUCTION

This appeal centers on a dispute between Governor Arnold Schwarzenegger and the State of California ("State")[1/] and the Rincon Band of Luiseno Mission Indians ("Rincon" or "Band") over the permissible scope of

1. Under article IV, section 19(f) of the California Constitution, the Governor is the only state official authorized to negotiate compacts with federally recognized tribes. Thus, the Governor and the State are one and the same insofar as the negotiation of compacts is concerned.

negotiations when a tribe requests an amendment to its existing tribal-state class III gaming compact. The disagreement the parties have over the permissible scope of amendment negotiations involves three issues. The first is the extent of the State's ability to request an increase in the amount of revenue Rincon would be required to share with the State in return for the Band's ability to extend the duration of its compact and to operate up to 900 additional slot machines free from non-tribal competition.[2/] The second is whether the Indian Gaming Regulatory Act, 25 U.S.C. § 2701 et seq. ("IGRA"), permits the State to earmark that revenue for the general welfare of its citizens. The third involves the appropriate remedy should a court determine that the State has inadvertently exceeded the permissible scope of negotiation.

Unlike compacts in six other states and more recent California compacts approved by the Secretary of the Interior (including compact amendments executed by Rincon's closest competitors), which require that tribes make general fund payments of up to 25 percent of the net win from slot machines, Rincon's compact ("Compact") requires no payments whatsoever to the State's

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2. The phrase "freedom from non-tribal competition" is hereafter sometimes referred to either as "exclusivity" or " amended exclusivity" depending upon whether the discussion relates to the Compact or Rincon's proposed amendment.

general fund in return for its ability to operate 1600 slot machines and other class III gaming with exclusivity. As a result, Rincon (with a membership of approximately 650) earned gross revenue of approximately $300 million in 2005 of which more than $59 million was profit.[3/] With an amendment on Rincon's terms, the Band could gross over $460 million, of which more than $93 million would be profit. (E.R. 1044-5.) Pursuant to section 4.3.2 of the Compact, such payments as the Band makes are deposited into the Revenue Sharing Trust Fund ("RSTF"). RSTF funds are paid to other federally recognized tribes operating no slot machines or fewer than 350 machines. Further, under the percentages set forth in Compact section 4.3.2.2 (a)(2), Rincon's current RSTF payments amount to no more than $1,335,000 per year which constitutes approximately one-half of one percent of the Band's gross revenues in 2005.

In the decision from which the Governor appeals, the district court granted Rincon's motion for summary judgment on the First Amended Complaint's ("FAC") Second Claim for Relief alleging that the Governor had negotiated over Rincon's amendment request in bad faith. The court held that even

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3. Rincon's slot machines averaged $381 in net win per day in 2005 (more than three and one-half times the net win for machines in Las Vegas). (E.R. 1035; 1041.)

though Rincon was asking to be freed from the restrictions in its Compact regarding duration and the number of authorized slot machines, the State was precluded from asking Rincon to increase the consideration it currently paid (in the form of revenue sharing) unless it offered the Band something other than more time and more machines.

Though the Governor, in fact, did offer Rincon an economic concession in addition to an increase in the duration of the Compact and the number of authorized slot machines (an automatic financial remedy in the event its exclusivity were lost)[4], the district court considered that concession to be premised on the occurrence of a "speculative and unlikely event" and, therefore, of "markedly lesser value" to the Band in relation to the size of the revenue share the Governor had requested (which the court deemed unreasonable) and the value of the concession the State had provided the Band when it entered into the Compact.

Additionally, the court concluded that there had to be a nexus between the State's use of the requested revenue sharing funds and a gaming related purpose and that because the revenue the Governor requested could be utilized for the general welfare of the State's citizens instead for "gaming-related

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4. This remedy is sometimes referred to in the record as "enhanced" or "geographic exclusivity."

interests," the revenue would not be utilized for an IGRA sanctioned purpose.

Finally, the district court concluded that because the revenue sharing the Governor had requested amounted to the imposition of a tax, the Governor had negotiated in bad faith.

The district court erred in concluding that the State cannot ask for general fund revenue sharing in return for agreeing to an increase in the scope and duration of Rincon's exclusivity. Article IV, section 19(f) of the California Constitution is an authorization providing the Governor with the authority to execute a compact, which is similar to an exclusive public franchise. While the Governor is precluded from seeking additional consideration for an existing compact, where as here, a tribe seeks to extend the duration and expand the scope of its existing compact, the Governor has a right to expect and receive additional consideration.

Further, the district court's conclusion that the revenue contribution the Governor requested was unreasonable in light of the fiscal benefit conferred upon Rincon is inconsistent with the holding in *In re Gaming Related Cases ("Coyote Valley II")*, 331 F.3d 1094, 1115 (9th Cir. 2003). The district court should have found the State's proposal reasonable because it utilizes a revenue sharing mechanism this Court approved in *Coyote Valley II* (net win percentage

increasing progressively as the number of authorized slot machines increases) and because use of the revenue sharing mechanism in the State's offer results in essentially the same level of contribution for 2500 slot machines as would the mechanism this Court approved in *Coyote Valley II.*

Similarly, the district court's conclusion that revenue sharing may only be utilized for a gaming related purpose is contradicted by this Court's contrary conclusion in *Coyote Valley II,* 331 F.3d at 1111-15. In that case, the Court approved a request for payments to the RSTF. The use of RSTF funds, however, is not limited to gaming related purposes but instead is unrestricted and may be utilized by Non-Compact Tribes for the general welfare of their members. This Court held that because the RSTF accomplished one of IGRA's objectives, which is the promotion of tribal economic development, self-sufficiency and strong tribal governments, payments to the RSTF were consistent with IGRA.

In this case, because general fund revenue sharing provides states with an incentive to give tribes exclusivity and because exclusivity vastly increases the revenue tribes can generate from gaming, such revenue sharing is likewise consistent with IGRA. Further, as this Court held in *Coyote Valley II,* in enacting IGRA, Congress "did not intend that States ignore their economic

interests when engaged in compact negotiations" (*id.*) and that (quoting from IGRA's legislative history) a "State's governmental interests with respect to class III gaming on Indian lands include... its economic interest in raising revenue for its citizens." *Id.* Thus, general fund revenue sharing not only promotes an IGRA purpose but is envisioned by that statute.

Finally, the district court's finding that the Governor had per se negotiated in bad faith simply because the requested revenue sharing contribution amounted, in the court's view, to the imposition of a tax, is inconsistent with the holding in *Coyote Valley II*, 331 F.3d at 1113 where this Court ruled that a state's request in negotiations for what amounts to a tax is merely "evidence" and not "conclusive proof" that the state has negotiated in bad faith. Thus, the district court erred in conducting no inquiry into the Governor's conduct apart from its analysis of whether the requested revenue sharing amounted to the imposition of a tax.

For these reasons, the State respectfully requests that this Court reverse the district court's decision on the basis that the Governor did not seek to impose a tax upon the Band and could seek general fund revenue sharing, or, in the alternative, remand the matter to the district court directing that it issue an order requiring the parties to resume negotiations in accord with ground rules

for negotiation established by this Court's decision, rather than the 60-day negotiation remedy applicable when the State has negotiated in bad faith.

STATEMENT OF JURISDICTION

The district court had jurisdiction over the FAC's Second Claim for Relief. That claim asserted that the State had breached the Band's Compact by failing to negotiate an amendment in good faith. In *Cabazon Band of Mission Indian v. Wilson,* 124 F.3d 1050, 1056 (9th Cir. 1997), this Court ruled that federal courts have jurisdiction over a suit seeking to enforce the terms of a tribal-state gaming compact pursuant to 28 U.S. C. §§ 1331 and 1362.

This Court has jurisdiction over the State's appeal pursuant to 28 U.S. C. § 1292, subdivision (a)(1) because the State filed its appeal on May 8, 2008, within 30 days of the district court's April 29, 2008, order and because that order is a permanent injunction that provides Rincon complete relief on the FAC's Second Claim for Relief.

ISSUES PRESENTED

1. Where Rincon seeks a Compact amendment that: (a) would free the Band from the restrictions the current agreement imposes on the number of slot machines it may operate; and (b) extend the duration of that agreement, did the district court err in concluding that the State sought to impose an impermissible

tax upon the Band when, in return for agreeing to Rincon's request and providing the Band with an economic remedy in the event Rincon's exclusivity were lost, the State asked the Band to make revenue sharing payments calculated on the basis of a formula (similar to the one approved by this Court in *Coyote Valley II*) that is based on a percentage of Rincon's net win from the operation of its authorized slot machines?

2. Where general fund revenue sharing provides states with an incentive to give tribes the exclusivity that vastly increases tribal revenues and where IGRA does not establish tribes as the sole beneficiary of class III gaming conducted pursuant to a compact and recognizes a state's right to negotiate both in furtherance of its economic interests and to raise revenue for its citizens, did the district court err in concluding the State negotiated Rincon's request for a Compact amendment in bad faith because the State requested revenue sharing payments that would provide for the general welfare of its citizens?

3. Where IGRA provides that a state's negotiation demand for direct taxation of a tribe is merely evidence, rather than conclusive proof, of a state's bad faith and where Ninth Circuit precedent holds that bad faith negotiation is not subject to "bright-line rules," did the district court err when it based its finding that the State negotiated Rincon's request for a Compact amendment in

bad faith solely upon its conclusion that the State's revenue sharing request constituted the imposition of a tax?

STANDARD OF REVIEW

Each of the issues presented was raised below and is addressed in the district court's decision. Each issues raises mixed questions of fact and law upon a stipulated record involving an interpretation of the Compact and IGRA and is reviewed de novo by this Court. *Coyote Valley II,* 331 F.3d at 1107.

STATEMENT OF THE CASE

In June, 2003, this Court, in *Coyote Valley II,* upheld the validity of two revenue sharing provisions contained in fifty-eight tribal-state class III gaming compacts executed in 1999 by the State of California and federally-recognized tribes with Indian lands in the State. Subsequent to this decision, Governor Arnold Schwarzenegger was elected and took office in November, 2003. Early in 2004, the Governor appointed a compact negotiator. This negotiator immediately commenced negotiations pursuant to requests by some of the fifty-eight tribes for an amendment that would allow them both to exceed the limit imposed by their existing compacts on the number of slot machines they could operate and to operate all of their existing slot machines for a longer period of years. Rincon is one of the tribes that requested negotiations.

Under its Compact, Rincon is precluded from operating more than 2000 slot machines and is unable, as a practical matter, to operate even that many devices under that agreement's terms. In this regard, Rincon's Compact requires it to obtain Gaming Device licenses through a draw process before it can operate more than 350 devices. Further, Rincon's Compact limits the total number of Gaming Device licenses that may be issued to all tribes in the State. Rincon is unable to obtain any such licenses because, few if any, licenses remain for issuance under the statewide limit and because of the preference the Compact license draw process gives to tribes that operate far fewer slot machines than Rincon does.

As a result, Rincon asked the State to agree to a Compact amendment that would free the Band from the Compact's restrictions on the number of slot machines it is authorized to operate and thereby enlarge Rincon's exemption from California's constitutional prohibition against casino-style gambling. Specifically, Rincon asked for an amendment that would extend the term of the Compact by up to fifty years and authorize Rincon to operate up to 2500 slot machines, with the potential to gross the Band more than $460 million per year from its Gaming Facility.

In responding to Rincon's request, the Governor relied upon this Court's decision in *Coyote Valley II*, 331 F.3d 1094. In particular, the Governor relied upon these holdings:

1. Congress in enacting IGRA "did not intend to require that States ignore their economic interests when engaged in compact negotiations" and that "IGRA's legislative history explains that a "State's governmental interests with respect to class III gaming on Indian lands include ... its economic interest in raising revenue for its citizens." *Id.* at 1115.

2. A state does not impose a tax, fee, charge, or other assessment upon an Indian tribe in contravention of 25 U.S.C. § 2710, subdivision (d)(4) when it offers an Indian tribe a "meaningful concession" in return for a payment that would otherwise amount to a tax, fee, charge, or other assessment. *Id.* at 1111, 1112.

3. The "exclusive right to conduct lucrative Las Vegas-style class III gaming, free from non-tribal competition" (*id.* at 1104) in "the most populous state in the country" (*id.* at 1115) is the "core" of what the tribe will receive from a compact (*id.* at 1104) and constitutes a "meaningful concession" by the State. This concession justifies a request for a revenue contribution that is based on a percentage of a tribe's net win that increases

progressively as the number of slot machines a tribe operates increases. *Id.* at 1115.

In conducting compact and compact amendment negotiations, the Governor also relied upon the fact that the *Coyote Valley II* decision expressed "no view" on the legality of a requirement that revenue sharing payments be deposited in a state's general fund (*Coyote Valley II,* 331 F.3d at 1115, n. 17) and that the compacts of six other states that had general fund revenue sharing provisions had already been approved by the Secretary of the Interior ("Secretary"). Indeed, the Governor's confidence in the legality of such provisions was further justified by the Secretary's approval of compacts and compact amendments containing general fund revenue sharing provisions that the Governor negotiated in 2004.

As a result, when Rincon asked to increase the extent and duration of its ability to conduct Las Vegas-style class III gaming free from non-tribal competition, the Governor responded with an offer that: (a) tracked what this Court had found consistent with IGRA and (b) corresponded with what the Secretary had approved in California and six other states regarding general fund revenue sharing provisions.

In *Coyote Valley II*, this Court approved two types of revenue sharing provisions. The first provision requires a payment by the tribes to the RSTF. This fund is administered by a State agency, the California Gambling Control Commission ("Commission"), and provides up to $1.1 million per year to each federally-recognized tribe in California that either did not operate slot machines or operated less than 350 such machines during the year. The amount a tribe is required to contribute depends on the number of Gaming Device licenses it possesses. That amount ranges from $900 to $4350 per license per year.

The second provision requires a payment to the Special Distribution Fund ("SDF"). This fund is controlled by the California Legislature and may provide funds to cover the State's costs of regulating tribal gaming, mitigating the adverse social, economic and environmental impacts associated with tribal gaming, to cover shortfalls in the RSTF, and to fund any other programs specified by the Legislature. The amount a tribe is required to contribute depends upon the number of Gaming Devices it operated prior to execution of the compact (September 1, 1999) and its net win per device. That amount is seven percent of net win for the 201st to 500th of those devices, ten percent of net win for the 501st to the 1000th of those devices, and thirteen percent of net

win for the 1001st to the 2000th of those devices. Tribes that operated fewer than 200 devices as of September 1, 1999, make no payments into the SDF. Rincon is one of those tribes.

The Governor's offer to Rincon agreed to extend the duration of Rincon's freedom from non-tribal competition, provide the Band with a monetary remedy that did not exist in its existing Compact should non-tribal competition occur, and authorize the operation of 900 additional slot machines. In return, the Governor asked that the Band continue contributing to the RSTF and maintain its existing Gaming Device licenses. In addition, the Governor requested that Rincon make payments to the State's general fund based upon the Band's net win. The amount requested was ten percent of the 2005 net win from the Band's existing 1600 slot machines and fifteen percent of the annual net win from any additional devices up to a total of 2500 devices. The Governor's offer, however, included a proposal that would provide Rincon with a credit against these revenue sharing amounts for payments the Band made to local governments addressing local adverse impacts. Based on revenue figures Rincon supplied to the Governor, whether the Band paid the requested sums according to an SDF style formula or the State's similar formula, the amount would total over $35 million per year.

Rincon rejected the Governor's proposal. In return for this amendment, which would free the Band from the slot machine licensing system established by its Compact, Rincon offered to continue to maintain its existing slot machine licenses and pay the fees associated with such licenses. It also agreed to pay fees related to the cost of regulating gaming and for the mitigation of the adverse social and environmental impacts of tribal gaming. What it agreed to pay, however, was far less than what Rincon's existing Compact required other tribes to pay for the same costs and impacts. It was also far less than what its closest competitors were paying under the terms of their recently amended compacts. In addition, Rincon's proposal did not permit the State to utilize the funds in the same manner it was able to under the existing Compact. Under the Compact, the California Legislature is entitled to appropriate SDF monies as it sees fit among the various listed programs in Compact section 5.1. Under Rincon's proposal, Rincon would be entitled to challenge the State's appropriation for the costs of regulating tribal gaming and had to approve, by means of a memorandum of understanding, any program addressing the adverse social, economic and environmental of tribal gaming. Furthermore, while tribes that pay for regulatory, mitigation and social impact costs under the 1999 compacts also pay into the RSTF for the benefit of other tribes, Rincon's

proposal substituted its payment to the RSTF for a payment for regulatory, mitigation and social impact costs.

The State rejected Rincon's proposals because they provided the State with no meaningful consideration in return for the State's agreement to free Rincon from the restrictions contained in the Band's existing Compact and to grant the Band additional rights.

STATEMENT OF FACTS

1. In September 1999, then Governor Gray Davis executed Rincon's existing Compact. (E.R. 1640.) The terms of that Compact are in all significant respects identical to the terms contained in compacts executed by Governor Davis and more than 60 other tribes. (*Id.* at 1640-41.) With respect to the number of Gaming Devices (slot machines) the tribes would be authorized to operate, the compacts guarantee each tribe the entitlement to operate 350 (or the number that tribe operated on the date the compacts were executed) (Compact § 4.3; E.R. 1112) without the necessity of licenses. In addition, the compacts allow tribes to obtain licenses to operate additional slot machines over and above the 350 device entitlement from a statewide pool administered by the Commission (Compact § 4.3.2.2; E.R. 1113). The compacts, however, limit the size of the statewide license pool and limit the

maximum number of slot machines a tribe can operate, either with or without licenses, to 2000. (*Id.*)

2. The compacts do not set forth a specific number for the size of the license pool. Instead, they provide a formula for calculating that number. (Compact § 4.3.2.2(a)(1); E.R. 1113.) In June 2002, in its implementation of duties and responsibilities with respect to the administration of the license pool under the compacts, the Commission calculated the size of the license pool at 32,151 licenses. (E.R. 1084-85; 1093-97.) Thereafter, on the basis of that calculation, the Commission began issuing licenses to tribes pursuant to a draw process that is also set forth in the compacts. (*Id.* at 1003.)

3. Though Rincon at one time possessed sufficient licenses to operate 2000 slot machines at its casino, for financial reasons it chose to return 400 of those licenses to the license pool in August 2002. (E.R. 1003.) Those 400 licenses were then issued to other tribes by the Commission under procedures specified in the Compact. By the time Governor Arnold Schwarzenegger was elected in November 2003, the licensing pool was essentially exhausted. As a result, tribes such as Rincon that desired additional licenses were unable to obtain them from the pool. (*Id.* at 1644.)

4. At this point, tribes in Rincon's position that wished to operate additional slot machines had two choices. Either they could negotiate amendments to their compacts that allowed them to obtain slot machines outside of the licensing pool, or they could pursue the argument as Rincon has chosen to do, that the Commission's calculation of the size of the pool was erroneous, and file suit seeking a judicial declaration that would increase the number of available licenses in the pool sufficiently to enable them to operate additional slot machines without first amending their compacts. (E.R. 1100.)

5. In 2004, a group of five tribes ("Five Tribes") sought to obtain authorization to operate additional slot machines by negotiating amendments to their compacts. The amendments those tribes negotiated with the State provided them with authority to operate additional slot machines without having to depend on the exhausted licensing pool or being subject to the 2000 per tribe limit and extended the duration of their compacts by 10 years. (E.R. 140-42, 170; 173-75, 203; 206-08, 236; 239-42, 269; 271,73, 301.) In return for these concessions by the State, those tribes agreed to certain revenue sharing provisions, additions to the environmental protection provisions of the compacts, and inclusion of certain other provisions designed to provide increased protection for patrons and employees of the casinos, as well as to

clarify ambiguous provisions of the compacts. (*Id.* at 139-301.) In addition, the Five Tribes specifically agreed to retain, and maintain through the required payment into the RSTF, their existing licenses from the pool established by the 1999 compacts. (*Id.* at § 4.3.1(a)(ii) of each compact.) The amendments were ratified by the Legislature and approved by the Secretary of the Interior as consistent with the requirements of IGRA. 69 Fed. Reg. 53733 (Aug. 27, 2004).

6. Rincon, however, chose to pursue both options simultaneously. Thus, while Rincon prepared to litigate the Commission's calculation of the size of the license pool, it also pursued Compact amendment negotiations intended to enlarge the number of slot machines available to it.

7. Rincon initially pursued a negotiation path with Governor Schwarzenegger. On November 21, 2003, it requested Compact amendment negotiations in a joint letter with ten other tribes. (E.R. 110.) The Governor's Office acknowledged receipt of that letter on December 16, 2003. (*Id.*) On January 7, 2004, the Governor appointed former California Court of Appeal Justice Daniel M. Kolkey as the State's compact negotiator and commenced negotiations with the Five Tribes and other tribes that had contacted Mr. Kolkey directly. (*Id.* at 131.)

8. Instead of contacting Mr. Kolkey after his appointment as negotiator to request a meeting date as had other tribes, Rincon sent a meet and confer letter to the State pursuant to Compact section 9.1 asserting that the State had breached the Compact by, among other things, failing to properly calculate the size of the licensing pool and failing to negotiate an amendment to the Compact in good faith. (E.R. 111-114.) While documents requested by the State were being compiled for the purposes of that meet and confer session, Rincon participated in compact amendment negotiations with the Five Tribes and the State's negotiator by attending a negotiation session on April 7, 2004. (*Id.* at 135.)

9. On April 21, 2004, Rincon requested separate negotiations. (E.R. 131-32.) Before that Compact amendment negotiation session was held, the meet and confer session requested by Rincon regarding the State's alleged Compact violations was held on June 2, 2004. (*Id.* at 120.) The meet and confer session ended without either party changing its legal positions. (*Id.* at 120-27.)

10. Thereafter, on June 4, 2004, at the first separate negotiation session between Rincon and Mr. Kolkey, Rincon stated that what it wanted from a Compact amendment were provisions that would allow it to obtain 400 more slot machines outside of the licensing pool which would increase its total

number of slot machines to 2000, while paying the same fee it would have paid if the authorization to operate those machines had come from the licensing pool. Moreover, instead of paying those fees to the RSTF for the benefit of Non-Compact tribes as would be required for pool licenses, Rincon wanted the fees for these devices to be earmarked for local projects that benefitted Rincon. (E.R. 132-33; 1654.) At the conclusion of that negotiation session, Rincon requested a further meeting in July, 2004. (*Id.* at 138.) Mr. Kolkey agreed to a July 1, 2004, session on the condition that the Band provide him with its negotiation proposals two weeks in advance. (*Id.*) The session was canceled after Rincon failed to provide any negotiation proposals whatsoever. (*Id.*)

11. Five days after the June negotiation session, instead of providing the State with a Compact amendment negotiation proposal, Rincon chose to file suit on June 9, 2004, asserting among other things that the State's license pool calculation was incorrect and that the State had failed to negotiate a Compact amendment in good faith.

12. On March 22, 2005, the district court dismissed Rincon's license pool claim for relief based on Rincon's failure to join the Five Tribes. (E.R. 1634-35; 60-68.)

13. Unable to obtain the 400 additional slot machines it sought through a direct challenge to the Commission's calculation of the size of the statewide licensing pool, the Band sought to acquire authority to operate additional slot machines indirectly through continued Compact amendment negotiation and its "bad faith negotiation" claim for relief. Seventeen months after the parties' last negotiation session, Rincon returned to the table for another Compact amendment negotiation session with the State's negotiator, on November 4, 2005. (E.R. 1659.)

14. However, instead of providing the State with a Compact amendment proposal, as the State's negotiator had requested earlier on June 4, 2004, Rincon insisted that the State make another offer first. The State, though not required to do so, obliged Rincon by making a new offer. (E.R. 357-60.) The terms of the State's offer were substantively similar to the terms that had been agreed to by the Five Tribes and approved by the Secretary of the Interior as consistent with IGRA. (Compare *id.* 139-301 to 357-60.) The State's proposal also reduced the revenue share proposal contained in its June 4, 2004, offer. Instead of asking for 15 percent of net win on all slot machines operated by the Band, the State's November 4, 2005, proposal requested only 15 percent of the Band's average net win on its slot machines in operation in 2004 (a fixed

sum) and 15 percent of the average net win on any additional slot machines (a sum that would fluctuate depending on the new machines' performance). Rincon did not make a counter- proposal at that meeting.

15. More than twenty-six months after it had first requested Compact amendment negotiations with the Schwarzenegger Administration on November 21, 2003, seventeen months after the first negotiation session between the parties on June 4, 2004, and nearly three months after the State's November 4, 2005, proposal, on January 25, 2006, Rincon made its first written Compact amendment proposal. The Band offered to pay the same fee per slot machine ($4350) that it would have had to pay if the machines were authorized by licenses from the Compact licensing pool. (E.R. 1660; 587-88; 581-86.) The Band's proposal thus sought to increase its slot machine authorization to 2500 machines by paying the same per-machine fee on the additional 900 machines as it was paying under the unamended Compact.

16. On January 27, 2006, the State rejected Rincon's proposal on the grounds that it offered nothing to the State in return for allowing Rincon to operate additional slot machines and was actually worse than Rincon's oral proposal that the State had rejected during the negotiation session in June 2004. (E.R. 589-92.) The State requested that Rincon reconsider its proposal. (*Id.* at

592.)

17. More than three months later, on May 5, 2006, the Band submitted another proposal. (E.R. 1661; 594-687.) By this proposal which again contemplated a total of 2500 slot machines, Rincon offered to pay the same fee per slot machine ($4350) that it would have had to pay if the machines were authorized by licenses from the compact licensing pool, for the right to operate the first 400 additional slot machines. (*Id.* at 595.) In return for the right to operate an additional 500 slot machines over and above 2000 devices, the Band offered to pay $6000 per additional device. (*Id.*) These fees, however, could only go to programs approved by Rincon. (*Id.*) Submitted with Rincon's proposal were certain financial data and legal analyses that Rincon asserted demonstrated that the State's prior proposals were not acceptable from a legal or financial standpoint. (*Id.* at 1660.)

18. In July 2006, Governor Schwarzenegger's Legal Affairs Secretary Andrea Hoch succeeded Mr. Kolkey as the State's negotiator for compacts and compact amendments. (E.R. 1663.)

19. After Ms. Hoch's appointment as negotiator, three meetings took place between Rincon and the State on August 9, 2006, September 12, 2006, and October 5, 2006. (E.R. 1664.) At these meetings, Rincon did not make any

Compact amendment proposals. Instead, Rincon focused its efforts on an attempt to convince Ms. Hoch that the Band's political makeup, geographic location, and competitive market made the State's prior offers financially unacceptable. (E.R. 915-1016.) Rincon urged Ms. Hoch to change the Commission's calculation of the number of Gaming Device licenses available under Compact section 4.3.2.2(a)(1). (*Id.* at 949-54.) The Band also asked that the State require the Five Tribes to return their Gaming Device licenses to the licensing pool for Rincon's benefit. (*Id.* at 1010-16.)

20. After a hearing on September 6, 2006, the district court set the date of November 3, 2006 as the close of Compact amendment negotiations between Rincon and the State for the purposes of this litigation. (E.R. 34(F).)

21. Because Rincon made no Compact amendment proposals at the August 9, September 12, or October 5, 2006, negotiations between the parties, the State asked the Band to provide it with a statement regarding what the Band wanted in a Compact amendment. In a letter dated October 12, 2006, the Band stated that it "wanted to protect the value of the 1999 Compact deal, which is for 2000 machines at the fee schedule set forth in Section 4." (E.R. 1017.) Rincon also announced that the only basis upon which it would consider more than a "modest" expansion would be if it were to develop a "second full service resort

(on reservation)," if the State were to agree to allow it to develop a casino at "a site with better market opportunity", or if "significant access and/or roadway improvements" were provided. (*Id.*)

22. On October 23, 2006, the State made yet another Compact amendment offer. (E.R. 1020-28.) In return for agreeing to grant Rincon a financial remedy for the loss of exclusivity ("geographic" or "enhanced" exclusivity), for allowing the Band to operate up to an additional 900 slot machines and for awarding Rincon a Compact extension of five years, the State requested a revenue share reduced to 10 percent of the average net win from the slot machines in operation at the Band's casino in 2005 and 15 percent of the average net win from any additional slot machines. The State also requested that the Band agree to essentially the same non-economic terms to which the Band's nearest competitors had agreed in their amended compacts. (*Id.*)

23. In the letter in which the State's October 23, 2006, offer was made, Ms. Hoch declined to repudiate the Commission's calculation of the statewide limit on the number of Gaming Devices or to require the Five Tribes to return the Gaming Device licenses to the licensing pool. (E.R. 1025-27.) In addition, though the State's offer to Rincon was for up to 900 additional slot machines and a five year extension, Ms. Hoch's letter indicated that, if Rincon were

interested, the State would be willing to make a proposal limited to an increase of 400 additional devices with no Compact extension. (*Id.* at 1025.)

24. On October 24, 2006, Rincon's counsel advised the State that though Rincon's May 5, 2006, offer was still what it was interested in, the Band was also interested in receiving a proposal from the State that involved an increase of 400 slot machines without a Compact extension. (E.R. 1029.)

25. The parties met again on October 26, 2006. (E.R. 1665.) Rincon made no counter-offer at that meeting.

26. On October 31, 2006, the State responded to Rincon's request and made an offer that limited the Band to 400 additional slot machines with no Compact extension. (E.R. 1032-33.) The State also provided the Band with an economic analysis of the financial implications of the State's October 23rd and October 31st offers. (*Id.* at 1035-1045.) That analysis, conducted by Professor William Eadington, demonstrated that Rincon was outperforming the average win per unit per day of its immediate competitors ($369 per day for Rincon versus an average of $336 for its competitors) (*id.*, at 1044) and that it would likely do better by accepting the State's offers than by rejecting them. (*Id.*, at 1044-45; 1037-38.) The State requested that the Band reply to its proposals by November 2, 2006, so that the State would have adequate time to prepare a

response before the Court-ordered negotiation record cut-off on November 3, 2006. (*Id.* at 1033.)

27. On November 3, 2006, Rincon rejected both the State's October 23, 2006, offer and the State's October 31, 2006, offer. In rejecting those offers, Rincon asserted that the State had failed to offer it a "meaningful concession" in return for any payments requested by the State. (E.R. 1066; 1665.) Rincon claimed that the State's offer of additional slot machines and a Compact extension provided it with nothing of value because it did not want an extension, the State constitution had already granted it exclusivity, and its "Compact already entitles Rincon to an additional four hundred (400) gaming devices." (*Id.* at 1665.)

28. On December 4, 2006, Rincon filed the FAC. (E.R. 1632.)

29. On December 15, 2006, the State filed its answer. (E.R. 1676.)

30. On June 1, 2007, Rincon and the State filed cross motions for summary judgment. (E.R. 9.)

31. On August 13, 2007, the district court heard oral argument on those motions. (E.R. 10.)

32. On April 29, 2008, the district court issued an order granting in part and denying in part the cross motions for summary judgment in which it

granted Rincon's motion for summary judgment on the Band's Second Claim for Relief and granted the State's motion for summary judgment on the remaining claims. (E.R. 9-33.)

33. On May 8, 2008, the State filed its appeal of the district court's order contained within its April 29, 2008 decision compelling the parties to follow the remedial process established by the Compact where it has been judicially determined that the State negotiated an amendment request in bad faith. (E.R. 1620.)

SUMMARY OF ARGUMENT

As a grant by the State of an authorization to operate a class III gaming monopoly, Rincon's Compact must be construed narrowly in favor of the State. Because the Compact contains no provision granting Rincon any right to renew the agreement for any period or to increase the number of slot machines it is authorized to operate on the same terms, the district court erred in reading into the Compact a right of renewal that would provide Rincon with the right to expand the scope and duration of its Compact on the same terms. Thus, contrary to the court's conclusion, it is Rincon - not the State - that is obligated to provide additional meaningful consideration in return for a Compact amendment.

The consideration the State sought in return for agreeing to Rincon's request is reasonable because it asks for the payment of fees in accord with a formula this Court approved as reasonable in return for the exclusive right to operate slot machines in the most populous state in the nation. *Coyote Valley II,* 331 F.3d at 1115.

The amended exclusivity provided by the extension and expansion of its monopoly provides Rincon with more revenue than it could achieve from class III gaming in the absence of that exclusivity. Payment into the State's general fund of the revenue sharing the State requested provides the State with an incentive to continue the Band's exclusivity and the increased revenue that exclusivity brings. General fund revenue sharing thus serves IGRA's purposes where, as here, it provides the Band with more revenue to accomplish that statute's objectives than would be the case in the absence of exclusivity. Further, nothing in IGRA bars the State from benefitting financially from tribal class III gaming where IGRA does not make tribes the exclusive beneficiaries of such gaming and recognizes that states may negotiate compacts to further their economic interests and to raise revenue for their citizens. Finally, the district court should have deferred to the Secretary's construction of IGRA in which the Secretary approved general fund revenue sharing compacts.

Assuming arguendo that the district court was correct in concluding that the State sought to impose a tax upon the Band, the court erred in basing its finding that the State had negotiated in bad faith solely on that fact. Under IGRA's plain language and this Court's holding in *Coyote Valley II,* 331 F.3d at 1113, a state's attempt to impose a tax upon a tribe is only evidence of bad faith negotiation – not conclusive proof of that act. Thus, a finding that a state has sought to impose a tax is only the beginning of a nuanced and fact-specific analysis regarding a state's good faith rather than its end. Where, as here, the State legitimately relied both upon the Secretary's approval of compact amendments with the same or similar terms and this Court's decision in *Coyote Valley II* and no appellate court has found the terms for which the State negotiated improper, the State should be found to have negotiated in good faith.

ARGUMENT

I.

THE COMPACT DOES NOT PROVIDE RINCON WITH A RIGHT TO EXPAND THE SCOPE AND DURATION OF ITS CLASS III GAMING MONOPOLY ON THE SAME TERMS. THUS, THE DISTRICT COURT ERRED WHEN IT FOUND THE STATE NEGOTIATED IN BAD FAITH BY ASKING RINCON FOR ADDITIONAL CONSIDERATION FOR SUCH AN EXPANSION

The district court's decision concludes that the State, in return for agreeing to an increase in the scope and duration of Rincon's Compact, may not ask Rincon to contribute more in revenue sharing than is provided for in the Band's Compact unless the State offers the Band something other than "more devices or time." (E.R. at 26.) Notwithstanding the fact that the Compact contains a specific termination date with no automatic right of renewal and expressly limits the number of slot machines the Band may operate for the term of the Compact, the district court construed the Compact to allow a potentially unlimited expansion of the scope and duration of Rincon's monopoly for the same consideration set forth in the Compact. (*Id.* at 26-7.)

Having interpreted the Compact in that fashion, the court then finds the State negotiated in bad faith by asking Rincon to increase its revenue sharing contribution without offering Rincon a meaningful concession in return. (*Id.* at

28-9.)

The district court misinterpreted both the nature and the meaning of the Compact and, in so doing, erred in concluding that the State had negotiated in bad faith.

A. As the Grant of a Monopoly, the Compact Must Be Construed Narrowly in Favor of the State

In upholding the validity of the 1999 compacts, this Court in *Artichoke Joe's California Grand Casino v. Norton,* 353 F.3d 712, 731 (9th Cir. 2003) described the compacts as the "award of exclusive class III gaming franchises." *Id.* This description echoes the district court's similar characterization in *American Greyhound Racing, Inc. v. Hull,* 146 F. Supp. 2d 1012, 1079 (D.Ariz 2001) (rev. on other grnds) where the court held that the award of tribal gaming compacts in Arizona constituted Arizona's "actions to convey an exclusive class III gaming franchise on tribes." *Id.* Indeed, the compacts are similar to an exclusive public franchise because they grant Rincon and other California federally-recognized Indian tribes the exclusive right to conduct class III gaming in California. As noted in Corpus Juris Secundum:

> A "franchise" has been defined as a privilege or special privilege conferred by government upon an individual, organization, or corporation, which does not belong to the citizenry at large, and in which activity one otherwise could not engage without the franchise. A franchise is a privilege of doing that which does not belong to citizens generally by

common right.

37 Corpus Juris Secundum 139 (2008).

Exclusive public franchises are construed narrowly in favor of the grantor and courts will not enlarge an exclusive franchise by implication. As the United States Supreme Court found in rejecting the notion that the grant of a franchise for thirty years created a perpetual franchise:

> The doctrine is firmly established that only that which is granted in clear and explicit terms passes by a grant of property, franchises, or privileges in which the government or the public has an interest. [Citations omitted.] Statutory grants of that character are to be construed strictly in favor of the public, and whatever is not unequivocally granted is withheld. [Citations omitted.] This principle, it has been said, "is a wise one, as it serves to defeat any purpose concealed by the skillful use of terms to accomplish something not apparent on the face of the act, and thus sanctions only open dealing with legislative bodies." *Slidell v. Grandjean*, 111 U. S. 412, 438, 4 Sup. Ct. Rep. 475.

Coosaw Mining Co. v. State of South Carolina, 144 U.S. 550, 561 (1892). *See also, Larson v. State of South Dakota,* 278 U.S. 429, 435 (1929) ("public grants are to be strictly construed, that nothing passes by implication to the grantee").[5/]

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5. Rincon argued in the district court that exclusivity was awarded by article IV, section 19(f) of the California Constitution approved by the voters rather than by the Compact. This rule of construction, however, is unaffected by whether exclusivity is awarded by the Compact or by the Constitution. Either must be construed narrowly in favor of the grantor -- the State.

B. The District Court Erred by Ignoring the Compact's Express Limitations and by Implying Non-Existent Terms

The district court erred both by ignoring the express limitations in the Compact and by construing the Compact expansively rather than narrowly when it determined that Rincon was entitled to free itself from the restrictions the Compact placed on the number of slot machines it could operate and for how long it could operate them upon payment of the same consideration required by that Compact for the operation of the Band's 1600 devices.

The Compact specifically provides that it will terminate on December 31, 2020, unless eighteen months prior to that date either party requests an extension of the Compact or a new compact. If a timely request has been made and no agreement has been reached before December 31, 2020, the Compact will terminate on June 30, 2022. (Compact Addendum A, Mod. 4, E.R. 1148.) The Compact also sets an express limit on the number of slot machines the Band may operate. Rincon is limited to no more than 2000 devices and may not operate more than 350 slot machines unless it receives a license for such a device from a limited pool of such licenses. (Compact § 4.3, E.R. 1112.) Further, the Compact contains no right to an automatic renewal of any of it terms. Thus, if a party requests a change in any Compact provision, it is required to negotiate for that change. (Compact §§ 12.0, 4.3.3, E.R. 1142;

1115.)

In this case, the district court essentially reversed the burden of providing consideration for a Compact amendment and placed it upon the State instead of Rincon. While recognizing that the Band sought an amendment allowing it to operate "additional gaming machines" as well as "an extension of its Compact terms by 25 years to year 2045" (E.R. 25), the court treated the State's request for consideration for that change as though it were a request by the State for an amendment to the Compact.[6/] The district court then found that the State failed to offer Rincon adequate consideration (meaningful concession) for the

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6. The district court stated it this way:
Rincon and the State already have an existing Compact that both Rincon and the State want to amend. Rincon seeks additional gaming machines and extension of its Compact term by 25 years to year 2045, while the State seeks substantial revenue sharing directly from the Tribe to the State's general fund. (E.R. 25.)

Indeed, the court ruled subsequently (quoting authority that a valid modification of a contract must be accompanied by consideration) that:

> In order to amend the existing Compact to properly allow for the State's new revenue sharing proposal, the State must provide other meaningful concessions to Rincon. The need for *other meaningful concession* is not only required under basic contract law principles governing modification, but the Ninth Circuit's interpretation of Section 2710(d).

(E.R. 26-7.) (Emphasis in original.)

amendment it sought because the State "simply offered more devices and time." (E.R. 26.)

Implicit in the district court's analysis (that freeing Rincon from the restriction on the number of slot machines it could operate and for how long it could operate them had little or no value) is a view of the Compact as an instrument that provides Rincon with a Compact right to operate any number of additional slot machines for any length of time without offering the State anything more than the RSTF contribution its current Compact would require. The court's decision, therefore, converts a Compact authorizing the operation of a limited number of devices for a limited term into one that permits the operation of an unlimited number of devices in perpetuity.[7/]

Nothing in the Compact authorizes such a conclusion.[8/] The mere fact

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7. While Rincon only asked for the right to operate an additional 900 devices and an extension of the Compact to the year 2045 (and a right to renew for an additional twenty-five years (E.R. 690), nothing in the district court's reasoning would preclude the Band from subsequently asking for another amendment that would permit the operation of an additional 900 devices to the year 2070. Again, in return for the State's concurrence, the Band would be required to pay nothing more than the existing Compact's level of consideration.

8. Assuming arguendo, that it is article IV, section 19(f), and not the Compact, that grants Rincon exclusivity, nothing in that constitutional provision states that a compact executed by the Governor and ratified by the Legislature will provide California Indian tribes the right to operate an unlimited number of slot machines in perpetuity. Indeed, at the time the voters approved the ballot proposition containing this constitutional provision, they had before them the

Rincon has the right to operate 1600 slot machines potentially until the year 2022 in return for contributions to the RSTF does not mean it is entitled to operate 2500 machines until the year 2045 for an RSTF contribution. Rincon's Compact does not contain a provision guaranteeing either an automatic renewal on the same terms or a right to operate additional devices on the same terms.[9] Indeed, nothing in the Compact provides that the State intended to foreclose its ability to ask for additional consideration in return for releasing Rincon from the restrictions contained in the Compact. Thus, the district court improperly read into the Compact provisions that simply do not exist or impermissibly inferred the existence of provisions in the grant of a monopoly. *Larson v. State of South Dakota,* 278 U.S. at 435.

C. The Consideration The State Requested For Releasing Rincon From the Compact's Restrictions Is Reasonable Because It Is Calculated on the Basis of a Formula Comparable to the One This Court Found Reasonable in *Coyote Valley II*

In *Coyote Valley II,* 331 F.3d at 1115, this Court held that where a tribe asked for and received the exclusive right to conduct class III gaming in the most populous state in the union (something IGRA did not contemplate and

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Compacts, which provide for a limited number of slot machines for a limited term.

9. For example, the Arizona gaming compacts at issue in *Am. Greyhound Racing, Inc. v. Hull,* 305 F.3d at 1023 provide for an automatic right of renewal.

that could not be achieved without the State's consent), the State was entitled to ask in return that the tribe make a revenue sharing contribution. The revenue sharing contribution the Court approved was based upon a percentage of a tribe's net win that increased as the number of slot machines in operation increased. *Id.*

In this case, neither IGRA nor Rincon's Compact contemplate any right to an extension on the same terms, or a right to operate additional machines on the same terms. Thus, the State has the same right to obtain consideration for its consent to Rincon's amendment request as it had to seek consideration for the establishment of the Band's monopoly in the first place. This is especially the case where, as here, in addition to providing Rincon with an extension of its monopoly and the additional machines the Band seeks, the State has offered to provide Rincon with a monetary remedy (absent from its Compact) in the event the Band's exclusivity is lost.[10/]

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10. In addition to consenting to the operation of Rincon's 1600 slot machines beyond the year 2022, and to the operation, for any period, of an additional 900 slot machines, the State agreed to provide the Band with a monetary remedy, not granted by its present Compact, for the loss of exclusivity. Under its current Compact, the Band's only option in the event of abrogation of its exclusivity is to terminate the Compact, and thus lose its right to conduct class III gaming. (Compact § 12.4 & Compact Addendum A, Modification 5; E.R. 1148-49.) The State's offer thus extends to the Band a significant monetary remedy not contained in its present Compact by proposing to allow it to continue to operate not only its existing slot machines, but the additional 900 machines as

In this instance, the level of revenue sharing the State requested in return for the amendment Rincon requested is entirely consistent with the Ninth Circuit's decision in *Coyote Valley II,* 331 F.3d at 1114-15 because it is calculated on the basis of a formula comparable to the one this Court found reasonable.

The Compact provides for SDF payments by tribes to the State. Those payments are calculated on the basis of a percentage of a tribe's net win in which the payment percentage increases as the number of slot machines the tribe operates increases. As a result, the SDF contribution for tribes operating more than 1000 devices is seven percent of net win for 201 to 500 devices, ten percent for 501 to 1000 devices, and thirteen percent for 1000 to 2000 devices. (Compact § 5.1(a), E.R. 1115.) In this case, the State utilized a similar formula in calculating the level of consideration it requested of the Band. If the result of the application of the SDF formula is compared to the total achieved by application of the State's formula (ten percent of net win on Rincon's existing 1600 devices and fifteen percent of the net win on the 900 additional devices Rincon seeks), the State's request with respect to 2500 slot machines asks Rincon to make a payment that would be roughly comparable to what a

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well, with a dramatic reduction in its payments to the State if its exclusivity is breached.

payment utilizing an SDF style formula would have been -- $35.8 million compared to $37.9 million.[11/] Because this Court found the SDF level of payment in return for an exemption from free market competition both reasonable and not inimical to IGRA's intent, the State's request is entitled to the same approval.[12/]

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11. The State does not suggest that Rincon could be required to make an SDF payment under its Compact. It could not. The State's point is that, in *Coyote Valley II*, this Court did not base its approval of the SDF formula on the fact it was only applied to pre-existing devices. The Court based its approval on its conclusion that a progressively increasing percentage of net win was appropriate in return for exclusivity. Utilizing the net win figures in the record (E.R. 1044) both a revenue sharing requirement based on an SDF style formula and the formula in the State's offer result in a revenue sharing payment in excess of $35 million per year. Based on a net win of $369/day, 7% of 201-500 machines equals $2,828,385; 10% of 501-1000 machines equals $6,734,250; and 13% of 1000 to 2500 machines equals $26,263, 575 for a total of $35,826,210. This is substantially the same as the $37.9 million payment the State's formula might require.

12. The court ruled as follows on this point:

> While the contributions tribes must make to the SDF are significant, the tribes receive in exchange an exclusive right to conduct class III gaming in the most populous State in the country. We do not find it inimical to the purpose or design of IGRA for the State, under these circumstances, to ask for a reasonable share of tribal gaming revenues for the specific purposes identified in the SDF provision.

Coyote Valley II, 331 F.3d at 1114-15. It bears noting in this regard, that in approving the SDF level of revenue sharing, the Ninth Circuit did not assert, and the State does not suggest, that this level constituted a cap on the level of revenue sharing a state could request, nor did the Court suggest that the SDF formula is the only acceptable revenue sharing formula.

Further, as the administrative record in this case reveals, casinos that are not protected from free market competition earn far less per slot machine per day than do Indian casinos that are protected from such competition by the terms of their compacts. Nevada casinos that are not protected from competition earn between $70 and $169 per slot machine per day (E.R. 1041) while tribal casinos in North County San Diego, in 2005, earned an average of $341 per slot machine per day. (*Id.* 1044.) Thus, the value of the protection afforded Rincon by an amended Compact that allowed it to operate 2500 slot machines beyond the expiration date of its existing compact could be upwards of three times or more than what the State asked from the Band.

As a consequence, the level of revenue sharing the State has requested of Rincon represents, in the words of this Court, a reasonable share of the Band's tribal gaming revenues in return for what the Band was asking to receive. *Coyote Valley II,* 331 F.3d at 1114-15.

Furthermore, the district court's conclusion that the consideration the State requested was unreasonable because the Band might receive "only" $60.9 million in profit or $1.716 million more than it currently earns from its Compact, while the State would receive $37.9 million more than it currently receives from that Compact (i.e. nothing), mis-perceives the appropriate

inquiry when judging what constitutes a reasonable consideration request. The relevant inquiry is not whether the tribe makes as great a profit as it would desire, but rather whether the percentage of net win requested by the State (10 and 15 percent) is reasonable in return for an extension of the Compact's term (Rincon asked for a 25-year extension with an automatic 25-year renewal), an increase in the number of authorized slot machines that could be operated pursuant to the amended monopoly granted by an amendment, and a previously unavailable financial remedy should the State end the monopoly by allowing non-tribal class III gaming.

Contrary to the district court's apparent conclusion, the State is not responsible for ensuring any particular level of tribal profit. The value of its offer to Rincon should not be based on any such preconceived level because it is the Band – not the State – that has predominant control over Rincon's profit margin. For example, in this case the Band's profit margin is directly affected by, among other things, its decision to continue to pay Harrah's Entertainment, the largest gaming company in the world, $36.3 million per year to manage its casino. (E.R. 1045.) Rincon's voluntary decision to pay that much money to Harrah's when other tribes, including its closest competitors, have chosen to manage their own enterprises is, of course, the Band's choice, but it is a choice

that plainly has an impact on Rincon's bottom line. Thus, it is not the State's proposal alone that leaves Rincon with the profit level of which the Band complains but rather, arguably, its voluntary decision to continue to operate in a manner different from other tribes by deliberately choosing to market its casino as a Harrah's property for a perceived economic advantage. There is no reason, in other words, that the State must assume that all of Rincon's other business decisions represent immutable costs and that it is up to the State to compensate completely for them when negotiating its revenue share. The State should not be penalized for the cost of Rincon's marketing choice when the State's offer is otherwise a reasonable proposal.

II.

GENERAL FUND REVENUE SHARING PROVISIONS ARE CONSISTENT WITH IGRA BECAUSE THEY PROVIDE STATES WITH AN INCENTIVE TO AWARD TRIBES EXCLUSIVITY WHICH, IN TURN, PROVIDES TRIBES WITH MORE REVENUE WITH WHICH TO ACCOMPLISH IGRA'S OBJECTIVES

The district court also found that the consideration requested by the State was improper because the proposed revenue contribution would be paid to directly to the State's general fund. (E.R. 30.) The court read 25 U.S.C. § 2710(d)(3)(C)(iii) as limiting a state's revenue sharing requests to amounts necessary to defray the costs of regulating tribal gaming activities where the

state did not offer a tribe a meaningful concession. (*Id.*) In addition, it found that where a state has offered a meaningful concession, IGRA only allows a state to request revenue contributions that will be paid for purposes consistent with IGRA, which it held were purposes that were related to tribal gaming. (*Id.*)

The district court misreads IGRA and misinterprets the import of this Court's decision in *Coyote Valley II* regarding the purposes to which an otherwise appropriate revenue sharing contribution may be put. The court's decision likewise ignores the import of the Secretary's approval of numerous compacts that require that tribal revenue contributions be paid into a state's general fund and fails to explain why it should not give deference to the Secretary's construction of IGRA. Similarly, the district court fails to recognize the fact that Congress, though expressly aware of the fact that numerous states are requiring that revenue sharing be placed into their general funds, did not bar that practice although the issue of amending IGRA for that purpose was before it.

A. The Payment of a Fee For the Operation of Slot Machines Is a Subject Directly Related to the Operation of Gaming Activities

IGRA, in section 25 U.S.C. § 2710(d)(3)(c)(vii), specifically provides that states may negotiate with tribes over "any other subjects that are directly

related to the operation of gaming activities." In this case, the State negotiated with Rincon over a fee for the operation of the Band's slot machines. That subject is directly related to the operation of Rincon's gaming activities and, thus, is a permissible subject for negotiation.

B. IGRA and Its Legislative History Demonstrate That States May Negotiate Compacts For the Purpose of Raising Revenue For Their Citizens

Nothing in IGRA controls a state's discretion with respect to the use of funds derived from gaming related activities. In this regard, while IGRA states that tribes are to be the "primary beneficiaries" of gaming activities, it does not make them the *sole* beneficiaries of such activities. *See* 25 U.S.C. § 2702(2) One of IGRA's purposes is to "ensure that the Indian tribe is the primary beneficiary of the gaming operation"). Thus, the Act envisions others benefitting financially from class III gaming.

As noted by this Court in *Coyote Valley II,* 331 F.3d at 1115, a review of IGRA's legislative history makes clear that Congress understood that a 'State's governmental interests with respect to class III gaming on Indian lands include . . . its economic interest in raising revenue for its citizens'" (*id.*), and its recognition that "Congress also did not intend to require that States ignore their economic interests when engaged in compact negotiations" (*id.*) Nothing in

this Court's description of IGRA's legislative history limits the nature of the economic interests for which a state is entitled to negotiate nor does it mention any limit on the purposes to which a state could put the revenue it raises for its citizens.

It is, of course, true that Congress did not intend for states to use compact negotiations as a "subterfuge for imposing State jurisdiction on tribes concerning issues unrelated to gaming." (*Coyote Valley II,* 31 F.3d at 1113.) A state, however, does not impose its jurisdiction upon a tribe at all when, as here, it provides a gaming related benefit (exclusivity and the enhanced financial rewards it provides) in return for an economic incentive that makes the provision of exclusivity financially rational for the state -- or, as in this case, continuing to make that benefit available.

Although this Court has considered significant the fact that any fees to be collected by a state would "go into the pocket of the State" (*Coyote Valley II,* 33 F.3d at 1113) in determining whether an otherwise appropriately sized fee is permissible, and though it has relied upon the fact fees would be put to gaming related purposes in considering whether fees were permissible, the Court has never held that gaming related fees utilized for a non-gaming related purpose are impermissible. *See id.* at 1115, n. 17.

When a state, in compact amendment negotiations, amends the provision of a benefit for which it was not required to negotiate, such as exclusivity, and provides a monetary remedy for the loss of that exclusivity, it cannot be said that the state is not acting in concert with the purposes of IGRA where the benefit, in fact, furthers IGRA's goal of " promoting tribal economic development, self sufficiency, and strong tribal governments" by greatly enhancing the amount of money the tribe could earn from gaming. Thus, giving states an incentive (through general fund revenue sharing) to offer the benefit of exclusivity or amended exclusivity to tribes, promotes IGRA's goals and objectives. As a result, where, as here, a state's revenue request in return for amended exclusivity results in a tribe earning more revenue from gaming than it could expect to receive from that activity in the absence of that exclusivity, the fact that the requested revenue will be utilized for the general welfare of a state's citizenry is consistent with IGRA's purposes. It bears noting, in this regard, that tribal members are also citizens of California and share in the public health, safety, transportation, educational, and other benefits general welfare spending provides.

Indeed, in *Coyote Valley II,* 331 F.3d 1111, this Court used the same rationale to support its conclusion that payments to the RSTF were consistent

with IGRA. As here, the use of RSTF funds is not limited to gaming related purposes, but instead is unrestricted and may be utilized for the general welfare of the members of Non-Compact Tribes. This Court held that because the RSTF accomplished one of IGRA's objectives, which is the promotion of tribal economic development, self-sufficiency and strong tribal governments, payments to the RSTF were consistent with IGRA. The Court said the following in that regard:

> Congress sought through IGRA to "promote[e] tribal economic development, self-sufficiency, and strong tribal governments." *Id.* § 2702(1). The RSTF provision advances this Congressional goal by creating a mechanism whereby *all* of California's tribes - not just those fortunate enough to have land located in populous or accessible areas - can benefit from class III gaming activities in the State.

Id. at 1111. (Emphasis in original.) Thus, even though the funds could be used by those tribes for non-gaming related purposes, the Court approved the mechanism because it furthered IGRA's objectives. Here, general fund revenue sharing furthers IGRA's objectives because it provides an incentive for states to offer the exclusivity or amended exclusivity that enhances tribes' financial rewards from class III gaming.

C. The District Court Should Have Deferred to the Secretary's Construction of IGRA and Recognized the Import of Congress' Failure to Bar The Practice Among States of Negotiating General Fund Revenue Sharing

In its decision, the district court essentially ignored the fact that, in addition to California, states such as Arizona, Connecticut, New York, New Mexico, Wisconsin and Michigan all have negotiated gaming compacts that require that tribal revenue sharing be deposited in either the states' general funds or for uses unrelated to gaming (E.R. 1718 et seq.) and that both the Secretary (with the authority to deny compacts deemed inconsistent with IGRA) and Congress have been well advised of this practice and have had the opportunity to prevent it, but have chosen not to do so. (*See* S. Hrg. 108-475, March 24, 2004; S. Hrg. 108-67, July 9, 2003.)

Prior to the approval of the first California compact amendments that contain revenue sharing provisions substantially similar to those at issue here, the Secretary required both the tribes and the State to justify such provisions. (E.R. 1728.) To date, the Secretary has approved numerous California compacts and compact amendments containing revenue sharing provisions similar to the provisions at issue in this case. The rationale for the Secretary's approval is set forth in an August 20, 2004, letter from the Secretary to Governor Schwarzenegger. (E. R. 1729-31.) In that letter, the Secretary

reaffirms the Department of the Interior's obligation to enforce the provisions of IGRA to ensure that tribes are not required to make payments to states that are prohibited by IGRA ("to enforce this statutory provision, the Department has sharply limited the circumstances under which Indian tribes can make direct payment to a State for purposes other than defraying the cost of regulating gaming activities"). The Secretary then goes on to conclude that:

> It is our determination that the revenue-sharing provisions described above are lawful under IGRA because the value of the exclusive gaming rights conferred on the Tribes is significant, and thus cannot be characterized as a prohibited tax pursuant to 25 U.S.C. § 2710(d)(4). *See In re Indian Gaming Related Cases,* 331 F.3d 1094 (9th Cir. 2003).

It is well established that where a statute contains ambiguous terms, courts will defer to the construction of that term by the agency charged with its implementation. *Thomas Jefferson Univ. v. Shalala,* 512 U.S. 504, 512 (1994); *Stinson v. United States,* 508 U.S. 36, 45 (1993). Here, the Secretary has determined that compacts containing revenue sharing provisions substantially similar to those at issue in this case are not inconsistent with IGRA. Because that construction constitutes a reasonable interpretation of the Act, this Court should defer to the Secretary's construction.

It is important to note, in this regard, that the Secretary's finding that revenue sharing provisions as consideration for the amended exclusivity

protection extended by the 2004 amendments does not constitute a prohibited tax was not predicated on the fact that the tribes had agreed to the State's terms. In the Secretary's view, such provisions are lawful because the value of the amended exclusive gaming rights conferred on the tribes is significant. Thus, the Secretary's finding that compacts with general fund revenue sharing requirements were consistent with IGRA stands independent of the fact those compacts were agreed to by the tribes and is just as applicable to proposed terms that a tribe refuses to accept as it is to terms it will accept. Given the Secretary's trust responsibility to tribes and the authority the Secretary possesses to enforce the provisions of IGRA, this Court should defer to the Secretary's conclusions regarding the legality of the payment of tribal revenues to the State's general fund irrespective of the fact that Rincon refused to agree.

Finally, the Secretary's approval of compacts containing general fund revenue sharing provision was well known to Congress at the time it held hearings on the subject matter of revenue sharing provisions in tribal-state class III gaming compacts. (*See* S.Hrg. 108-475, March 24, 2004; S. Hrg. 108-67, July 9, 2003.) Under basic rules of statutory construction, "Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change."

Lorillard v. Pons, 434 U.S. 575, 580 (1978). Thus, the fact that subsequent to hearings on the subject of general fund revenue sharing requirements in compacts, Congress failed to repudiate the Secretary's construction should be considered as further evidence that the Secretary's construction of IGRA by the approval of compacts containing such provisions is consistent with that statute.

III.

ASSUMING ARGUENDO THE STATE SOUGHT TO IMPOSE A TAX, THE DISTRICT COURT ERRED IN RELYING UPON THAT FACT ALONE TO CONCLUDE THAT THE STATE HAD NEGOTIATED IN BAD FAITH

The district court concluded that the State negotiated in bad faith solely on the basis of its finding that the State's request for "such a large fee to its general fund in return for concessions of markedly lesser value was in bad faith in light of the prohibition against taxation set forth in IGRA." (E.R. 30-31.) The court erred in resting its finding of bad faith negotiation on that fact alone because even if the revenue sharing request amounted to a proposed tax, the mere fact that a state has sought to impose a tax is only *evidence* that a state has negotiated in bad faith -- not conclusive proof that it has.

A. The District Court Erred in Treating Its Finding That the State Had Sought to Impose A Tax Upon the Band As Conclusive Proof the State Had Negotiated in Bad Faith

Though several courts have concluded that a state has negotiated in bad faith when it has refused to negotiate because there can be no good faith negotiation where a state has failed to negotiate at all (*see Mashantucket Pequot Tribe v. Connecticut,* 913 F.2d 1024, 1032 (2d Cir. 1990)), under the plain language of 25 U.S.C.§ 2710(d)(7)(B)(iii)(II) and this Court's holding in *Coyote Valley II,* 331 F.3d at 1112-13), there can be no per se bad faith if the state has engaged in negotiations but has merely exceeded the parameters of permissible negotiation under IGRA.

There is a fundamental difference between a refusal to negotiate and a failure to conduct negotiations in good faith. IGRA, in 25 U.S.C. § 2710(d)(7)(B)(ii)(II), describes two different bases for finding that a state has failed to negotiate in good faith. It provides that the burden of proof is on the state to demonstrate it has negotiated in good faith in two circumstances. The first is when a tribe alleges that a state "did not respond to the request of the Indian tribe to negotiate such a compact." The second is where the state "did not respond to such request in good faith."

In the first case, if a state has failed to negotiate at all, courts have found that unless the state was correct in its conclusion that it did not have to negotiate, its failure to negotiate constituted bad faith negotiation per se because one cannot be said to have negotiated in good faith if there has been no negotiation at all. *Mashantucket Pequot Tribe v. Connecticut,* 913 F.2d at 1032. In such a case, the fact that a state had a good reason to believe it was correct was deemed irrelevant because the failure to negotiate is automatically bad faith.

The second case presents an entirely different situation. Where a state has negotiated, no court has adopted a per se rule. In that scenario, as the Ninth Circuit held in *Coyote Valley II,* 331 F.3d at 1113, "the good faith inquiry is nuanced and fact-specific, and is not amendable to bright-line rules." (*Id.*)

As a result, the district court erred in failing to conduct such an inquiry.

B. The State's Reliance Upon the Secretary's Approval of Compact Amendments With Similar Revenue Sharing Provisions As Well As the Secretary's Approval of General Fund Revenue Sharing Compacts in Other States Precludes a Finding That the State Negotiated in Bad Faith

A requirement that a court, in conducting a good faith inquiry, examine the totality of the circumstances surrounding a negotiation is consistent with similar inquires in other negotiation contexts. In the labor relations context,

courts have made it clear that good faith is a state of mind determined by the objective facts surrounding a negotiation as gleaned from the record of the negotiations. *Seattle-First National Bank v. National Labor Relations Board,* 638 F.2d 1221, 1226 (9th Cir. 1981); *NLRB v. Fitzgerald Mills Corporation,* 313 F.2d 260, 266 (2nd Cir. 1963). Thus, the inquiry is always about the motives and intentions of the party as evidenced by the record. Moreover, in the absence of a contrary statutory intent, a statutory obligation to negotiate in good faith does not compel agreement. *National Labor Relations Board v. Tomco Communications, Inc.,* 567 F.2d 871, 884 (9th Cir. 1978) ("But the obligation to bargain collectively 'does not compel either party to agree to a proposal or require the making of a concession.'") Thus, good faith negotiation contemplates the possibility of an impasse. *Serramonte Oldsmobile, Inc. v. National Labor Relations Board,* 86 F.3d 227, 232 (D.C. Cir. 1996.) Moreover, the fact that a party to a negotiation has made a proposal based on industry practice or what others in comparable situations have accepted, has been considered to establish that the offer has been made in good faith. *National Labor Relations Board v. Tomco Communications, Inc.,* 567 F.2d at 884 n. 13.

In analyzing the State's conduct of negotiations, the district court should have utilized these principles to conduct the type of analysis conducted by Judge Wilken in *Big Lagoon Rancheria v. State of California,* No. C 99-04995 (E.R. 1750-51). In that case, the court refused to issue an order initiating the IGRA remedial process because of its determination that the State had reason to believe that its conduct was appropriate based on a prior judicial ruling and because the extent of the State's authority to negotiate for environmental mitigation was unsettled.[13/]

Here, the same situation is presented. On the general fund issue, the Ninth Circuit left the door open for the State to ask that revenue sharing be placed in

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13. In that case, Judge Wilken found that a negotiation request inconsistent with IGRA did not warrant a finding of "bad faith" where the law was uncertain. The court said the following in this regard:

> While it appears that the State has not negotiated with the Tribe in good faith thus far, a final determination of bad faith is premature at this time due to the novelty of the questions at issue regarding good faith bargaining under IGRA. Further, this Court's March 22, 2000 Order gave the State reason to believe that it could negotiate on environmental and land use issues. While the Tribe is correct that this was dicta, and the issue was not briefed by the parties at the time, this dicta nevertheless provided the State with a reasonable basis for its belief that it could negotiate environmental and land use issues with the Tribe in good faith. The Court's ruling today provides the State with guidance in further negotiations with the Tribe.

Big Lagoon Rancheria v. State of California, (citation omitted) (E.R. 1750-51).

the general fund by its ruling in *Coyote Valley II,* 331 F.3d at 1015 n.17. Likewise, given that the level of revenue sharing the Ninth Circuit approved as consistent with IGRA, among other things, is roughly equivalent to the level of revenue sharing the State requested of Rincon in this case, coupled with the Secretary's approval of similar conduct in six other states and the fact that no appellate decision had found it bad faith for a state to request revenue sharing, the State had ample reason to believe its conduct was consistent with IGRA.

Thus, the State's negotiating conduct in this case, even if ultimately found to be inconsistent with IGRA, should not be found to constitute bad faith negotiation. Indeed, to do otherwise would be to distort the plain meaning of the term good faith beyond all recognition by defining good faith to mean strict liability for any mistake of law.

CONCLUSION

For all the foregoing reasons, the State respectfully requests that this Court reverse the district court's decision and order entry of judgment in favor or the State, or, in the alternative, order that the district court require the parties to resume negotiations in accord with the principles enunciated in this Court's decision.

Dated: August 22, 2008

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CERTIFICATE OF COMPLIANCE WITH
RULE 32(a) For Case Number

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1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(A)(7)(B) because:

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Dated: August 22, 2008

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DECLARATION OF SERVICE BY OVERNIGHT COURIER

Case Name: **Rincon Band v. Schwarzenegger, et al.**

Court: **United States Court of Appeals, Ninth Circuit, Case No. 08-55809**

I declare:

I am employed in the Office of the Attorney General, which is the office of a member of the California State Bar, at which member's direction this service is made. I am 18 years of age or older and not a party to this matter; my business address is: 110 West A Street, Suite 1100, P.O. Box 85266, San Diego, CA 92186-5266. I am familiar with the business practice at the Office of the Attorney General for collection and processing of correspondence for overnight mail with **FEDERAL EXPRESS**. In accordance with that practice, correspondence placed in the internal mail collection system at the Office of the Attorney General is deposited with the overnight courier that same day in the ordinary course of business.

On **August 22, 2008**, I served the following documents:

APPELLANTS' OPENING BRIEF; AND APPELLANTS' EXCERPTS OF RECORD, VOLUMES I -VIII

by placing a true copy thereof enclosed in a sealed envelope with postage thereon fully prepaid, in the internal mail collection system at the Office of the Attorney General at 110 West A Street, Suite 1100, P.O. Box 85266, San Diego, CA 92186-5266, addressed as follows:

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In addition, I transmitted a true copy of the APPELLANTS' OPENING BRIEF via electronic mail as follows:

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I declare under penalty of perjury under the laws of the State of California the foregoing is true and correct and that this declaration was executed on **August 22, 2008**, at San Diego, California.

Roberta L. Matson
Declarant

Signature

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