UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF MICHIGAN

KEWEENAW BAY INDIAN COMMUNITY, Plaintiff, v. KHOURI, et al., Defendants.	File No. 2:16-cv-00121 Hon. Paul L. Maloney

MEMORANDUM IN SUPPORT OF PLAINTIFF'S MOTION FOR PARTIAL SUMMARY JUDGMENT

ORAL ARGUMENT REQUESTED

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Statement of Issues

1. In light of the categorical federal-law prohibition of state taxation of trade with Indians in Indian country, may Defendants impose the Michigan Sales Tax with respect to purchases made by the Keweenaw Bay Indian Community ("the Community") and its members on the Community's Reservation and trust lands?

   Most Apposite Authority: The Indian Trader Statutes, 25 U.S.C. §§ 261-264; *Central Machinery Co. v. Arizona State Tax Commission*, 448 U.S. 160 (1980); *Warren Trading Post Co. v. Arizona Tax Commission*, 380 U.S. 685 (1965).

2. In light of the categorical federal-law prohibition of state taxation of an Indian tribe or tribal member with respect to activities within Indian country, may Defendants impose the Michigan Use Tax with respect to property principally housed, garaged, and stored by the Community or its members within the Community's Reservation and trust lands?

   Most Apposite Authority: *Okla. Tax Comm'n v. Chickasaw Nation*, 515 U.S. 450 (1995); *Okla. Tax Comm'n v. Sac & Fox Nation*, 508 U.S. 114 (1993).

3. By imposing significantly greater burdens on the Community and its members in their exercise of federal-law tax immunities than are imposed on other entities or people exercising tax immunities or exemptions, does Defendants' Sales and Use Tax Refund and Exemption Process deprive the Community and its Members of their rights to due process and equal protection, as guaranteed by the Fourteenth Amendment to U.S. Constitution?

   Most Apposite Authority: *Gratz v. Bollinger*, 539 U.S. 244 (2003); *K.G. Urban Enterprises, LLC v. Patrick*, 693 F.3d 1 (1st Cir. 2012).

INTRODUCTION

Under long-settled rules of federal law, the Keweenaw Bay Indian Community (the "Community"), its members, and their vendors enjoy absolute immunity from state sales and use taxes with respect to the purchase or use of tangible personal property and services by the Community and its members within the Community's reservation and trust lands (the "Reservation").[1] The State of Michigan, through Defendants Nick A. Khouri, Walter A. Fratzke and Ruth Johnson (hereafter collectively "Defendants"),[2] acting in their official capacities, have systematically flouted this federal immunity, illegally imposing the Michigan sales tax on vendors for sales made to the Community and its members within the Reservation, and the Michigan use tax on the Community and its members with respect to property used within the Reservation.[3] Adding insult to injury, Defendants purport to consider, under a formal process, refund or exemption requests from the Community and its members with respect to these clearly exempt transactions, but then routinely reject such requests after long delays based on rote explanations that have no basis in federal law. Accordingly, this Court should enter partial summary judgment in favor of the Community on Counts I and V of the Third Amended Complaint, holding that federal law prohibits enforcement of the Michigan Sales and Use Tax Acts with respect to the purchase, lease, rental, and use of property and services by the

[1] The Community's Third Amended Complaint also includes claims regarding the State's enforcement of state tobacco laws in violation of federal law. Those claims are not part of this motion.

[2] Defendants Croley, Grano, and Sproull do not have any official role in enforcing the sales and use taxes and their actions are not at issue with respect to this motion.

[3] The Court can resolve the Community's claims regarding enforcement of the Michigan Sales and Use Tax Acts on the Reservation as a matter of law. The Community also alleges that enforcement of these acts in the ceded area under the Treaty of 1842 is also unlawful, but resolution of that issue will require additional discovery and possible expert testimony.

Community and its members within the Reservation, on Counts VII and VIII, holding that the formal refund and exemption process is also unlawful with respect the purchase, lease, rental, and use of property and services by the Community and its members within the Reservation, and with respect to Count XVII, issuing an injunction prohibiting application of the taxes or refund and exemption process.

STATEMENT OF UNDISPUTED FACTS

I. THE PARTIES.

A. The Keweenaw Bay Indian Community is Federally-Recognized Indian Tribe.

The Community is a federally-recognized Indian tribal government, organized and operating under a Constitution and Bylaws approved by the Secretary of the Interior on December 17, 1936, pursuant to the Indian Reorganization Act of 1934, 25 U.S.C. § 476 (recodified at 25 U.S.C. § 5123). Swartz Decl. ¶ 2.[4] The Community is the successor in interest to the L'Anse and Ontonagon bands of Chippewa Indians. *Id*. The Community exercises powers of self-governance and sovereign jurisdiction over the L'Anse and Ontonagon Indian Reservations, which are located on both sides of the Keweenaw Bay of Lake Superior in Baraga County, Michigan, as well as over other lands held in trust for the Community by the United States outside the Community's Reservations in the Upper Peninsula of Michigan. *Id*. ¶¶ 2, 5. The L'Anse and Ontonagon Reservations and these trust lands constitute "Indian country" within

[4] For this Motion, the Community relies upon the Declarations of Warren C. Swartz, Jr. ("Swartz Decl."), Susan J. LaFernier ("S. LaFernier Decl"), Michael J. LaFernier ("M. LaFernier Decl."), Elizabeth Mayo ("E. Mayo Decl."), Scott Mayo ("S. Mayo Decl."), and James K. Nichols ("Nichols Decl.") and the exhibits attached thereto.

the meaning of 18 U.S.C. § 1151.[5] The Community has approximately 3,625 enrolled members, approximately 1,044 of whom live on the Reservation. *Id.* ¶ 3.

B. Defendants Administer and Enforce the Sales and Use Taxes.

Defendant Nick A. Khouri is the Treasurer of the State of Michigan. In this capacity, Defendant Khouri oversees the Michigan Department of Treasury (the "Department"), the State agency that administers and enforces the Sales and Use Tax Acts. Answer to TAC ¶ 7, PageID.865. Defendant Walter A. Fratzke is the Department's Native American Affairs Specialist and oversees the administration of state laws involving Michigan taxes, including sales and use taxes, with respect to Michigan tribes and tribal members. *Id.* ¶ 8 PageID.865. Defendant Ruth Johnson is the Secretary of State of the State of Michigan. In this capacity, she oversees the Michigan Department of State, which manages and administers various programs and services, including motor vehicle registration, licensing, and the collection of certain taxes and fees. *Id.* ¶ 9 PageID.866.

II. THE DEPARTMENT IS ILLEGALLY TAXING THE COMMUNITY AND ITS MEMBERS' TRANSACTIONS.

The Community and its members have purchased, leased, rented, and used within the Reservation a wide variety of goods and services, and they expect to continue to do so. Swartz Decl. ¶ 7; S. LaFernier Decl. ¶ 3; M. LaFernier Decl. ¶ 3; E. Mayo Decl. ¶ 3; S. Mayo Decl. ¶ 3.

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[5] The definition of "Indian country" for federal law purposes includes "(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 border 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." Land held in trust for a tribe by the United States constitutes "Indian country" under this definition. *Oklahoma Tax Comm'n v. Sac & Fox Nation*, 508 U.S. 114, 124-25 (1993); *Oklahoma Tax Comm'n v. Citizen Band Potawatomi Indian Tribe of Oklahoma*, 498 U.S. 505, 511 (1991).

The goods and services involved in these transactions include, without limitation, motor vehicles, office furniture and equipment, household appliances and furnishings, clothing, gas, electricity, telephone and other telecommunications services, food and beverages served at restaurants and other establishments, and other items used in everyday life. Swartz Decl. ¶ 7; S. LaFernier Decl. ¶ 3; M. LaFernier Decl. ¶ 3; E. Mayo Decl. ¶ 3; S. Mayo Decl. ¶ 3; Nichols Decl. Ex. 1 (Summary Chart).

A. The Michigan Sales Tax Act.

The Michigan Sales Tax Act, Mich. Comp. Laws §§ 205.51-205.78 (the "Sales Tax Act") imposes upon all persons engaged in the business of making retail sales a tax equal to 6% of the gross proceeds from retail sales, leases, and rentals of tangible personal property in the State of Michigan. Mich. Comp. Laws § 205.52; *see also id.* § 205.51(1)(b) (defining "retail sale" as "a sale, lease, or rental of tangible personal property for any purpose other than for resale, sublease, or subrent"). "Tangible personal property" means "personal property . . . that is in any manner perceptible to the senses" and includes, among other things, electricity, water, gas, steam, and prewritten computer software. *Id*. § 205.51a(q).

The Sales Tax Act provides for a number of exemptions from the sales tax. The Act provides that if the seller obtains identifying information and the basis for the exemption claim from the purchaser and maintains a record of exempt transactions, the seller will not be liable for the tax if a purchaser improperly claims an exemption, unless the seller has committed fraud or has solicited the purchaser to make an improper exemption claim. Mich. Comp. Laws § 205.62.

For purposes of applying the Michigan sales tax, the location of a sale generally is the place where the product is received by the purchaser or the purchaser's designee. Mich. Comp. Laws § 205.69(1). If the place-of-receipt rule does not apply, then the location of the sale generally is the purchaser's address. *Id*.

B. The Michigan Use Tax Act.

The Michigan Use Tax Act, Mich. Comp. Laws §§ 205.91-205.111 (the "Use Tax Act") imposes upon each person a tax "for the privilege of using, storing or consuming tangible personal property" and for certain specified services in the state equal to 6% of the price of the property or services. Mich. Comp. Laws § 205.93(1). The Michigan use tax does not apply to property upon which the Michigan sales tax has been paid. *Id*. § 205.94(1)(a). The use tax is imposed on, among other things, the use, storage, or consumption of motor vehicles in Michigan if purchased, leased, or rented out of state or in an isolated sale in Michigan by a nonretailer, the use of certain telephone and other telecommunications services, and the use of hotel lodging services. *Id*. §§ 205.93(1) and (2), 205.93a(1)(a) and (b), 205.93c; Mich. Admin. Code R205.13(2). The Use Tax Act also presumes that tangible personal property purchased, leased, or rented outside of Michigan is subject to use tax if brought into Michigan within 90 days of the purchase date. Mich. Comp. Laws § 205.93(1)(a). Although the Michigan use tax is imposed on the consumer, a seller who is engaged in the business of selling tangible personal property for storage, use or consumption in Michigan is required to collect the use tax from the consumer. *Id*. § 205.95(1).

The Use Tax Act provides for a number of exemptions from use tax. The Use Tax Act states that if the seller obtains identifying information and the basis for the exemption claim from the purchaser and maintains a record of exempt transactions, the seller will not be liable for the tax if a purchaser improperly claims an exemption, unless the seller has committed fraud or has solicited the purchaser to make an improper exemption claim. Mich. Comp. Laws § 205.104b.

For purposes of applying the Michigan use tax, the location of a sale generally is where the product is received by the purchaser or the purchaser's designee. Mich. Comp. Laws § 205.110(1) (if the place of receipt rule does not apply, then the location of sale generally is the

purchaser's address). For most leased or rented property for which a lessor has elected to pay use tax on rental receipts,[6] the location of the transaction for the first lease payment is determined in the same manner as for a sale and therefore generally is the place where the property is received by the purchaser or the purchaser's designee. *Id*. § 205.110(2). Subsequent lease payments generally are sourced to the primary property location for each period covered by the payment as indicated by the address of the property provided by the lessee. *Id*.

III. THE COMMUNITY'S PRIOR LITIGATION REGARDING THE SALES AND USE TAX ACTS.

In 2005, the Community filed a lawsuit against the Treasurer of the State of Michigan, the Administrator of the Collection Division of the Michigan Department of Treasury, the Native American Affairs Specialist of the Michigan Department of Treasury, and the Secretary of State of Michigan. *Keweenaw Bay Indian Cmty. v. Kleine*, No. 2:05-CV-224 (W.D. Mich., filed Sept. 16, 2005). The lawsuit sought, among other things, declaratory and injunctive relief from the imposition and collection of Michigan sales and use taxes on purchases, leases, rentals, use, storage, or consumption by the Community or its members of tangible personal property or services within the Reservation. The Community's claims involving Michigan sales tax rested on the well-established federal law that states are barred from imposing any significant burdens, and certainly from imposing any direct tax, upon an Indian trader trading with reservation Indians. *E.g.*, *Central Machinery Co. v. Arizona State Tax Comm'n*, 448 U.S. 160, 165 (1980). The Community's claims involving Michigan use tax rested on the well-established federal law that states are barred from imposing a tax upon tribal or tribal member property located in Indian

[6] Lessors engaged in the business of renting or leasing tangible personal property to others may elect to pay use tax on rental receipts in lieu of paying sales or use tax on the full cost of the property at the time it is acquired. Mich. Comp. Laws § 205.95(4).

country, or the use of such property unless the taxing statute provides a mechanism for apportionment such that the tax only applies to activity outside of Indian country. *E.g.*, *Oklahoma Tax Comm'n v. Sac & Fox Nation*, 508 U.S. 114 (1993).

In the 2005 action, the parties filed cross motions for summary judgment on the merits of the Community's claims, but the District Court did not resolve the underlying substantive legal questions. Instead, acting *sua sponte*, the District Court dismissed the Community's claims as unripe, stating that "[t]he Court will not make abstract pronouncements of law about different types of activities until the Court is presented with a specific purchase or use for which the State has denied a tax exemption." *Keweenaw Bay Indian Cmty. v. Kleine*, 546 F. Supp. 2d 509, 526 (W.D. Mich. 2008) (2:05-cv-00224 PageID.2414). The Community appealed this decision to the Sixth Circuit. *Keweenaw Bay Indian Cmty. v. Rising*, 569 F.3d 589 (6th Cir. 2009). The Sixth Circuit affirmed on ripeness grounds, but further stated that "[i]f the Community files, and the State denies, a request for an exemption or refund based on a transaction occurring within Indian country and involving a member of the Community, the courthouse doors will be open to an appropriate challenge." *Id.* at 592-93. The Sixth Circuit further noted that "Michigan's briefs and statements at oral argument may misstate the law in certain respects, such as the preemptive effect of the Indian trader statutes, 25 U.S.C. §§ 261-264, or the necessity of apportioning the use tax under certain circumstances." *Id*. at 592.

IV. DEFENDANTS ENFORCE THE SALES AND USE TAX ACTS WITH RESPECT TO THE COMMUNITY'S AND ITS MEMBERS' PURCHASES AND USE OF PROPERTY AND SERVICES.

Since the 2009 Sixth Circuit decision, contrary to federal law but consistent with the positions taken in their previous briefs and at oral argument before the Sixth Circuit, Defendants have enforced the Sales and Use Tax Acts with respect to the purchase, lease, rental, use, consumption and storage of tangible personal property and services by the Community and its

members within the Reservations.

A. The Exemption and Refund Process.

After the Sixth Circuit decision, the Department established a formal process pursuant to which Michigan tribes without a formal tax agreement with the State, such as the Community, and members of such tribes, must file claims with the Department in order to seek an exemption or refund with respect to purchases, leases, rentals, use, storage, or consumption of property or services within Indian country ("the Refund and Exemption Process"). Swartz Decl. ¶¶ 9-12. Under the Refund and Exemption Process, tribes and tribal members can either pay Michigan sales and use tax and file a refund claim or request an advance determination that the particular transaction is not subject to tax.[7] Swartz Decl. ¶ 9; Nichols Decl. Ex. 2 (Form 4765) at SOM-FED00000012, Ex. 3 (Form 4766) at SOM-FED00000014. If an advance determination from the Department is not obtained, the purchaser must pay the tax at the time of sale and then submit a claim for refund of the tax paid. Swartz Decl. ¶ 9; Nichols Decl. Ex. 2 (Form 4765) at SOM-FED00000012; Ex. 3 (Form 4766) at SOM-FED00000014.

To seek an exemption, for each item purchased or to be purchased, the Department requires the requester to provide a variety of information to the Department about the purchaser, the item purchased, the location of various aspects of the transaction, seller information, and intended use of the item. Nichols Decl. Ex. 2 (Form 4675) at SOM-FED00000013; Ex. 3 (Form

[7] The Department created special forms for this process involving subject Indian tribes and tribal members. Nichols Decl. Ex. 2 (Form 4675) at SOM-FED00000012; Ex. 3 (Form 4766) at SOM-FED00000014. These claim forms, Form 4766 for tribes and Form 4765 for tribal members, are significantly longer and more intrusive than the Form 3372, "Michigan Sales and Use Tax Certificate of Exemption," that the Department uses in other, non-tribal situations in which purchasers may claim an exemption from the Michigan sales or use tax, and under the Refund and Exemption Process, the Department must rule upon each specific transaction, rather than allowing purchasers to simply provide a blanket exemption certificate directly to the retailer. *Id.* Ex. 5 (Form 3372) at 1.

4766) at SOM-FED00000016. For claims for refund, the Department also requires the requester to include documentation showing that sales or use tax was paid. Nichols Decl. Ex. 2 (Form 4675) at SOM-FED00000013; Ex. 3 (Form 4766) at SOM-FED00000016. The requester must then mail the completed refund claim form to the Department for consideration. Nichols Decl. Ex. 2 (Form 4675) at SOM-FED00000013; Ex. 3 (Form 4766) at SOM-FED00000016. This Exemption and Refund Process also includes guidelines for processing and deciding claims that the Department contends are based on federal law. Nichols Decl. Ex. 4 (Department Guidance) at SOM-FED00000018. Neither the claim forms nor the guidelines provide any timeline within which the Department must make a determination on the claim. *Id*.

Early on, the Community raised a number of objections to and concerns regarding the Refund and Exemption Process, but these fell on deaf ears; the Department refused to make any changes to the process. Swartz Decl. ¶ 10; Nichols Decl. Ex. 31 (W. Fratzke Ltr. Nov. 14, 2013).

B. Exemption and Refund Claims by the Community and Its Members.

Since July 2012, the Community and four tribal members submitted approximately 1,339 claims for exemption or refund to the Department ("Exemplar Claims"). Swartz Decl. ¶ 11; Nichols Decl. Ex. 1 (Summary Chart).[8] These Exemplar Claims relate to purchase and use of a wide variety of property and services, including motor vehicles, office furniture, equipment, and supplies, electronics and electrical parts, linens and uniforms, housekeeping items, appliances,

[8] With roughly 1044 members living on the Community's Reservation and Trust Lands, the number of transactions for which exemptions or refunds could be sought would far exceed the 1,339 Exemplar Claims. Swartz Decl. ¶ 12. Pursuant to Federal Rule of Evidence 1006, the Community has prepared a summary of the voluminous documentation of the Exemplar Claims identifying the claimant, the date of the claim, the goods or services purchased or leased, the Department's response to the claim, and the date of that response. Nichols Decl. ¶ 2; Ex. 1 (Summary Chart).

clothing, prepared food and beverages, auto parts and supplies, household goods and furnishings, nonprescription medications, toiletries, telephone and other telecommunications services, and gas, electricity, and similar goods and services. Nichols Decl. Ex. 1 (Summary Chart). All Exemplar Claims involve purchases and use within the Reservation, based on established Michigan rules for determining the location of a transaction for tax purposes (and under contract law principles). Swartz Decl. ¶ 7; S. LaFernier Decl. ¶ 4; M. LaFernier Decl. ¶ 4; E. Mayo Decl. ¶ 4; S. Mayo Decl. ¶ 4; Mich. Comp. Laws § 205.69(1) (sales tax); § 205.110(1) (use tax); *see also* Michigan Revenue Administrative Bulletin No. 2015-25 at 4 (Dec. 12, 2015) (leased goods).

All Exemplar Claims were made under protest, because the Community and its members object to the necessity of participating in the Refund and Exemption Process in order to exercise well-established federal immunities from state taxation. Swartz Decl. ¶¶ 9-11*; see also e.g.*, Nichols Decl. Ex. 7 (9-10-2014 Claim)[9] at SOM-FED00010870. Of the 1,339 Exemplar Claims, the Department denied approximately 1,185 claims, granted approximately 133 claims, and has failed to rule on approximately 21 remaining claims. Nichols Decl. Ex. 1 (Summary Chart). On average, the Department took 49 days to respond to an Exemplar Claim. *Id*.

C. The Department's Handling of the Exemplar Claims.

1. Claims Evaluated by Department as Sales Tax Claims.

In its decisions on the Exemplar Claims treated by the Department as involving sales tax, the Department has purported to apply the balancing test set forth in *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980). Defendants contend that, in their consideration of the

[9] The Exemplar Claims submitted as exhibits to the Declaration of James K. Nichols are referred to by date of purchase for refund claims, and date of submission for exemption claims. Each exhibit includes the claim documentation and Defendants' response.

refund applications, the Department balances all tribal, federal, and state interests based on the circumstances of each transaction. Nichols Decl. Ex. 6 (Defs. Disc. Resp.) at Resp. Interrog. No. 12. In fact, the Department has denied *all* the claims treated as sales tax claims except those involving purchases of property for use in what the Department views to be an "essential government function." Nichols Decl. Ex. 6 (Defs.' Disc. Resp.) at Defs. Resp. Interrog. No. 1.

The denied sales tax Exemplar Claims include the following:

- *all* Community claims for items purchased, leased, or rented within the Reservation for use in its gaming or other tribal revenue raising enterprises (*E.g.*, Nichols Decl. Ex. 8 (10-8-2015 Claim) at SOM-FED00008409 (Ojibwa Casino purchase of natural gas from SEMCO); Ex. 19 (1-31-2014 Claim) at SOM-FED00008515 (Ojibwa Casino purchase of various wall signs); Ex. 10 (6-19-2014 Claim) at SOM-FED00009325 (Ojibwa Hotel purchase of electrical parts));
- *all* Community claims for payments made through the Community Assistance Program ("CAP") on behalf of individual Community members for purchases of electricity and gas within the Reservation (*E.g.*, Nichols Decl. Ex. 12 (4-3-2014 Claim) at SOM-FED00005171-75 (CAP purchase of natural gas from SEMCO for Community member)); and,
- *all* Community member claims for purchases, leases, and rentals within the Reservation (*E.g.*, Nichols Decl. Ex. 7 (9-10-2014 Claim) at SOM-FED00010868-76 (member purchase from Bay Auto Parts); Ex. 13 (11-18-2012 Claim) at SOM-FED00012335-3 (member purchase from Walmart.com); Ex. 6 (Defs.' Disc. Resp.) at Resp. Interrog. No. 1 (Defendants do not recognize any Michigan sales tax exemption for purchases by Community members from any

retailer not wholly-owned by the Community or its members)).

All the Department's denial letters repeated the same rationale with only minor variations:

> The State clearly has jurisdiction to tax a non-Indian retailer operating in Michigan. Such taxes are used to fund state and local services for this and other businesses as well as Michigan's residents (including tribal members). These services are provided to the retailer regardless of the tribal status of its customers. On the contrary, there is no material impediment to tribal sovereignty by the imposition of Michigan's tax on the non-Indian retailers who may sell to individual tribal members. Given these facts, and after balancing all interests, it is clear that the State's interests are sufficient to justify its tax and thus, your sales tax refund is denied.

Nichols Decl. Ex. 12 (4-3-2014 Claim) at SOM-FED00005171-72; *see also*, *e.g.*, Ex. 7 (9-10-2014 Claim) at SOM-FED00010868. No denial letter even purported to address any federal interests, any tribal interests other than tribal sovereignty, much less address the specific circumstances of any particular transaction. *E.g.*, *id*. Exs. 7 (9-10-2014 Claim) at SOM-FED00010868-69; 8 (10-8-2015 Claim) at SOM-FED00008409-10; 10 (7-2-2014 Claim) at SOM-FED00009325-26; 12 (5-14-2014 Claim) at SOM-FED00005171-72.

The Department used almost exactly the same language in a letter denying the Community's claim for the purchase of natural gas for the Community's Casino, but added the following sentence: "*In addition, State interests are significantly harmed where the Tribe is able to market its exemptions via commercial activities that compete against non-Indian competitors.*" Nichols Decl. Ex. 8 (10-8-2015 Claim) at SOM-FED00008409 (emphasis added). The Department did not explain how the Community could have "marketed an exemption" where it was the purchaser that bore the direct economic burden of the sales tax.

2. Claims Evaluated by the Department as Use Tax Claims.

Defendants claim that the Community and its members are exempt from the use tax only if the property at issue "is used, stored, or consumed *solely* in the Community's Indian country."

Nichols Decl. Ex. 6 (Defs.' Disc. Resp.) at Resp. Interrogatory No. 3. Thus, in addressing the Exemplar Claims that it treated as use tax claims, the Department has granted claims involving telecommunications services. *E.g.*, Nichols Decl. Ex. 17 (4-15-2013 Claim) at 1-3, 9 (refund granted for Ojibwa Hotel purchase from Baraga Telephone)). But the Department has denied all other claims, including:

- *all* Community member claims involving purchases of motor vehicles, on the basis that the motor vehicle will be used in part outside the Community's Reservation (*E.g.*, Nichols Decl. Ex. 14 (10-3-2012 Claim) at SOM-FED00011473);
- *a* Community member claim involving a purchase of clothing, on the basis that the clothing "has been, or will be, used, stored or consumed" in part outside the Community's Reservation (Nichols Decl. Ex. 18 (11-26-2012 Claim) at SOM-FED00012376); and,
- *all* Community claims for items leased from an out-of-state lessor, on the basis that the lessor is considered the user of the items for state law purposes, even though the lessor is not using the item and may not even be located within Michigan. (*E.g.*, Nichols Decl. Ex. 15 (5-19-2015 Claim) at SOM-FED00008783-85 (denial of Community refund request for use tax paid on leased dishwasher)).

3. Consistency in Treatment of Claims as Sales Tax Claims or Use Tax Claims.

The Department determined whether to treat each Exemplar Claim as a claim relating to sales tax or to use tax, and its treatments were often inconsistent when the Community and its members purchased goods on the Reservation from a seller located outside of Michigan. For

example, of the eleven Exemplar Claims involving purchases of goods from Quill.com, four were treated as use tax claims and were granted, and seven were treated as sales tax claims and were denied. Nichols Decl. Ex. 1 (Summary Chart) at lines 960, 1143, 113-64, 1210, 1224, 1240, 1244-46, and 1259; *e.g.*, *id*. Ex. 21 (5-15-2015 Claim) (treated as use tax); Ex. 22 (2-25-2016 Claim) at SOM-FED00008373-79 (treated as sales tax). Twenty-four more Exemplar Claims involving purchases of goods on the Reservation from out-of-state sellers American Hotel Register and QVC were treated as use tax claims and were allowed (*id*. Ex. 1 (Summary Chart) at lines 61, 77, 116, 240, 393, 747, 1131, 1136, 1145, 1174, 1192, 1200-01, 1215, 1226, 1232, 1275, 1279, 1284, 1291-92, 1308, 1324, and 1330; *e.g.*, *id*. Ex. 23 (10-6-2016 Claim) at 1-3, 10; Ex. 24 (8-22-2016 Claim) at 1-2, 5), and eighteen more Exemplar Claims involving such purchases from out-of-state sellers Agilysis, American Solutions for Business, Harbor Linen, National Geographic Society, Qubica, Spartan Promotion, Under Armour, and Walmart were treated as sales tax claims and were denied (*id*. Ex. 1 (Summary Chart) at lines 45, 52, 100, 131, 192, 604, 614, 1091, 1098, 1153, 1170, 1173, 1231, 1247, 1307, and 1327; *e.g.* , *id.* Ex. 25 (11-9-2016 Claim) at 6-7; Ex. 26 (3-31-2016 Claim) at SOM-FED00009749; Ex. 27 (12-6-2012 Claim) at SOM-FED00012291). Although three Exemplar Claims involving purchases on the Reservation from out-of-state seller American Hotel Register were allowed, the Department has not yet ruled on three more Exemplar Claims involving purchases from American Hotel Register, the oldest of which was submitted fourteen months ago. *Id*. Ex. 1 (Summary Chart) at line 1267.

4. Timeliness of Decisions and Refunds.

Though the vast majority of the Department's actions on Exemplar Claims were rote denials based on stereotyped rationales, the Department usually took several weeks to issue them, and some claims were pending for over eight months before the Department took any

action.[10] *See* Nichols Decl. Ex. 1 (Summary Chart) at lines 4, 54-58, 62-64, 67-69, 1196-99. For example, the Department frequently took weeks or months to issue denials of the more than 700 Exemplar Claims involving natural gas purchases from SEMCO. *E.g.*, *id*. (Summary Chart) at lines 55, 64, 95. In one case the Community submitted a refund request for its payment of tax on a natural gas purchase for a member on May 28, 2013, and the Department took until November 7, 2013 to deny the request—164 days. *Id*. Ex. 16 (5-28-2013 Claim) at SOM-FED00001636-38. On average, the Department took 49 days to respond to claims by the Community and its members. In a number of instances, the Department altogether failed to rule or otherwise respond. *E.g.*, *id*. Ex. 1 ("Summary Chart") at lines 16, 142-43, 146-48.

In the few cases where Defendants did *approve* refunds, they did not necessarily *pay* the refunds. For example, on September 8, 2017, Defendants notified the Community that they would be issuing refunds on three claims made in 2013. Nichols Decl. ¶ 5. Defendants had previously approved, but never paid, refunds for those claims. *Id*. Ex. 1 (Summary Chart) at lines 72, 75, 199. There are likely other examples of refund claims approved but not paid, but it is virtually impossible to reconcile Defendants' approval of a refund with payment of the refund. The approval letters are sent separately from the refund checks, the checks often cover more than one claim, and the Department does not include any transmittal communication identifying the covered claims. *E.g.*, *id*. Ex. 28 (4-17-2015 Claim) at 8-9 (Refund Check and "Remittance Advice"); Swartz Decl. ¶ 11.

STANDARD OF DECISION AND ESTABLISHED LEGAL PRINCIPLES REGARDING

[10] Defendant Fratzke stated in an affidavit filed in the 2005 lawsuit that "once Treasury is provided with adequate information, it can usually provide a determination regarding the taxable status of a sale within a day or two." Nichols Decl. Ex. 30 (Fratzke Affidavit). With respect to the 1,339 Exemplar Claims filed over the course of five years, not once did the Department respond to a claim "within a day or two." *Id*. Ex. 1 (Summary Chart) Column "Days Elapsed" (shortest response time was seven days).

TAXATION IN INDIAN COUNTRY

I. SUMMARY JUDGMENT STANDARD.

Summary judgment is proper if "there is no genuine dispute as to any material fact" and judgment is appropriate as a matter of law." *Babcock & Wilcox Co. v. Cormetech, Inc.*, 848 F.3d 754 (6th Cir. 2017) (quoting Fed. R. Civ. P. 56(a)). The moving party bears the initial burden of demonstrating the absence of any genuine issue of material fact and its entitlement to judgment as a matter of law. *Celotex Corp. v. Catrett*, 477 U.S. 317, 323 (1986). To defeat the motion, an opponent may not rest upon the mere allegations or denials of his pleadings, but must set forth, through competent and material evidence, specific facts showing that there is a genuine issue of material fact for trial. Fed. R. Civ. P. 56(e); *Mounts v. Grand Trunk Western R.R.*, 198 F.3d 578, 580 (6th Cir. 2000). The nonmovant must do more than present a scintilla of evidence or cast metaphysical doubt as to the material facts; there must be evidence on which the jury could find for the nonmovant. *Matsushita Electric Ind. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986); *Nernberg v. Pearce*, 35 F.3d 247, 249 (6th Cir. 1994); *Street v. J.C. Bradford & Co.*, 886 F.2d 1472, 1479-80 (6th Cir. 1989).

II. ESTABLISHED LEGAL PRINCIPLES REGARDING TAXATION IN INDIAN COUNTRY.

A. Federal Law Regarding Taxes, Such as the Sales Tax, Where the Legal Incidence of the Tax Falls on a Non-Indian Seller.

The Indian Trader Statutes, 25 U.S.C. §§ 261-264, categorically bar a state from imposing a tax, the legal incidence of which falls on an Indian trader, for sales, leases, or rentals of property to Indian tribes or tribal members within their Indian country. These statutes state unequivocally that the Commissioner of Indian Affairs has "the sole power and authority to appoint traders to the Indian tribes and to make such rules and regulations as he may deem just and proper specifying the kind and quantity of goods and the prices at which such goods shall be

sold to the Indians." 25 U.S.C. § 261. Pursuant to this and other sections of the Indian Trader Statutes, the Commissioner has issued detailed regulations that govern all aspects of trading with reservation Indians. *See, e.g.*, 25 C.F.R. §§ 140.1-140.26. None of these regulations allows for the imposition of a state sales tax on an Indian trader with respect to sales of goods to Indian tribes or their members within the tribe's reservation or trust lands.

The Supreme Court repeatedly has held that the Indian Trader Statutes bar a state from imposing any significant burdens, and certainly from imposing any direct tax, upon an Indian trader trading with reservation Indians. In *Warren Trading Post Co. v. Arizona Tax Commission*, the Supreme Court unanimously held that the Indian Trader Statutes barred the imposition of an Arizona gross receipts tax upon a licensed Indian trader operating within the Navajo Indian Reservation. 380 U.S. 685, 690 (1965). The Indian trader, Warren Trading Post, was "a normal retail store" that sold "the necessities of life," such as "food, clothing, equipment," and "harnesses and seed" to Indians and non-Indians. Oral Argument at 0:31:31-49; 49:17-50:25, *Warren Trading Post Co. v. Ariz. Tax Comm'n*, 380 U.S. 685 (1965) (No. 115), https://www.oyez.org/cases/1964/115. Arizona sought to impose its gross receipts tax upon Warren Trading Post's gross income from sales on the Navajo reservation to reservation Indians. *Warren Trading*, 380 U.S. at 686 n.1. The Court held that the state tax could not be imposed on the Indian trader with respect to such sales, concluding that the all-inclusive nature of the Indian Trader Statutes and related regulations showed that "Congress has taken the business of Indian trading on reservations so fully in hand that no room remains for state laws imposing additional burdens upon traders." *Id.* at 690. The Court added that the "financial burdens" imposed by such a tax on an Indian trader or its Indian customers "could thereby disturb and disarrange the statutory plan Congress set up in order to protect Indians against prices deemed unfair or

unreasonable by the Indian Commissioner." *Id.* at 691.

Fifteen years later, in *Central Machinery Co. v. Arizona State Tax Commission*, the Supreme Court confirmed the federal preemption of state taxes imposed on Indian traders, regardless of whether the trader in question was licensed as an Indian trader. 448 U.S. 160, 165 (1980). In *Central Machinery*, Arizona sought to impose the same gross receipts tax at issue in *Warren Trading* upon a one-time sale of tractors by an Arizona corporation to Gila River Farms, a "business enterprise" of the Gila River Indian Community operating on the Gila River Reservation. Oral Argument at 0:00:40-54, *Cent. Mach. Co. v. Ariz. State Tax Comm'n*, 448 U.S. 160 (1980) (No. 78-1604), https://www.oyez.org/cases/1979/78-1604; 448 U.S. at 164 n.3. Unlike the Indian trader in *Warren Trading*, the seller in *Central Machinery* did not maintain a place of business on the Reservation and had not obtained an Indian trader license. 448 U.S. at 165. The Court nevertheless held that the state tax could not be imposed on the Indian trader, concluding that the Indian Trader Statutes "apply no less to a nonresident person who sells goods to Indians on a reservation than they do to a resident trader." *Id.* Dismissing the fact that the vendor lacked an Indian trader license, the Court held that "[i]t is the existence of the Indian trader statutes . . . and not their administration, that pre-empts the field of transactions with Indians occurring on reservations." *Id.*

More recently, in *Department of Taxation v. Milhelm Attea & Bros., Inc.*, the Supreme Court reaffirmed the federal preemption of direct taxation of Indian traders. 512 U.S. 61, 73 (1994). The case involved the New York cigarette tax statute, which required wholesalers who sold unstamped cigarettes to Indian tribes or reservation retailers to comply with certain record keeping, reporting, and substantiation requirements. *Id.* at 64. Several cigarette wholesalers who sold tobacco to Indian retailers challenged these administrative requirements as a violation of the

Indian Trader Statutes. *Id.* at 67-68. The Court upheld the administrative duties imposed on the wholesalers/Indian traders but, in doing so, sharply distinguished them from a direct tax. The Court emphasized that the administrative burdens placed on the Indian traders, in connection with a tax imposed on non-Indian retail purchasers, stood "on a markedly differing footing from *a tax imposed directly on Indian traders*, on enrolled tribal members or tribal organizations, or on 'value generated on the reservation by activities involving the Tribes.'" 512 U.S. at 73 (emphasis added) (quoting *Wash. v. Confederated Tribes of Colville Indian Reservation*, 447 U.S. 134, 156-57 (1980)).

Based on *Warren Trading* and its progeny, the Indian Trader Statutes absolutely bar a state from imposing a direct tax upon an Indian trader trading with reservation Indians.

B. Federal Law Regarding Taxes, Such as the Use Tax, Where the Legal Incidence of the Tax Falls on an Indian or Tribe.

Under well-established federal law, the imposition of a state tax the legal incidence of which falls upon an Indian tribe or tribal member with respect to activities within Indian country violates the Supremacy Clause in Article VI of the United States Constitution, and is therefore categorically barred as a matter of federal law. *Okla. Tax Comm'n v. Chickasaw Nation*, 515 U.S. 450, 458 (1995). With respect to property principally housed, garaged, and stored by an Indian tribe or tribal member within Indian country but used both within and outside Indian country, a state is without power to impose a tax upon the property or the use thereof, unless the taxing statute provides a mechanism for apportioning the tax to exclude the activity within Indian country from the reach of the tax. *Okla. Tax Comm'n v. Sac & Fox Nation*, 508 U.S. 114, 128 (1993); *Colville*, 447 U.S. at 163; *Moe v. Confederated Salish & Kootenai Tribes of Flathead Reservation*, 425 U.S. 463, 480-81 (1976); *Chosa v. Mich. Dep't of Treasury*, Mich. Tax Tribunal Dkt. No. 283437 (Apr. 20, 2005) (courtesy copy included as Addendum A to Nichols

Declaration).

In *Moe*, the Supreme Court barred the imposition of Montana's personal property tax on motor vehicles owned by tribal members who lived on the tribe's reservation and drove their vehicles both on and off the reservation. 425 U.S. at 480-81. Montana assessed the tax annually based on the value of the vehicle, and payment of the tax was made a condition precedent for registration of the vehicle. *Id*. at 468-69. The Court held that the tax could not validly be imposed with respect to the tribal members' vehicles. *Id.* at 480-81.

The Supreme Court reaffirmed the *Moe* holding in *Colville*. That case involved the State of Washington's motor vehicle excise tax, an annual tax based on the value of the vehicle, which was imposed for the privilege of using the vehicle in the state. 447 U.S. at 142-43, 162. The state imposed the tax on motor vehicles owned by tribal members who lived on the tribe's reservation and drove their vehicles both on and off the reservation. Washington attempted to distinguish its tax from Montana's personal property tax by describing it as an excise tax imposed for the "use" of the vehicles in question within the state. *Id.* at 163. The Supreme Court concluded that this purported distinction was meritless, and held that the inherent taxation of the on-reservation use of such vehicles rendered the entire tax invalid as applied to the tribal members:

> We do not think that *Moe* and *McClanahan* can be this easily circumvented. While Washington may well be free to *levy a tax on the use outside the reservation* of Indian-owned vehicles, it may not under that rubric accomplish what *Moe* held was prohibited. Had Washington tailored its tax to the amount of *actual off-reservation use*, or otherwise varied something more than nomenclature, this might be a different case.

Id. at 163-64 (emphases added).

In *Oklahoma Tax Commission v. Sac & Fox Nation*, the Court removed any doubt that, absent tailoring of a use tax to the actual amount of off-reservation use, states are absolutely

precluded from imposing use taxes upon Indian property that is principally housed or stored within Indian country. 508 U.S. at 127-28. The case involved Oklahoma's excise tax and registration fee on motor vehicles owned by tribal members who lived within the tribe's Indian country and drove their vehicles inside and outside Indian country. *Id*. at 119. Oklahoma imposed its excise tax, *inter alia*, "upon the use" of any vehicle; its registration fee, likewise, had the features of a use tax. *Id*. The excise tax was imposed on a one-time basis as a percentage of the value of the vehicle; the registration fee was imposed annually as a percentage of the value of the vehicle. *Id.* at 119-20. The Supreme Court unanimously held that Oklahoma's one-time tax and annual registration fees "are no different than those in *Moe* and *Colville*," emphasizing that both taxes were "imposed for use both on and off Indian country." *Id.* at 127. As the Court explained:

> Tribal members who live in Indian country consisting solely of scattered allotments likely use their cars more frequently on state land and less frequently within Indian country than tribal members who live on an established reservation. Nevertheless, members of the Sac and Fox Nation undeniably use their vehicles within Indian country. As we said in *Colville*, had the State "tailored its tax to the amount of actual off-[Indian country] use, or otherwise varied something more than mere nomenclature, this might be a different case. But it has not done so, and we decline to treat the case as if it had." 447 U.S., at 163-64 . . . .

Id. at 128 (bracketing in original).

Finally, in *Chosa v. Michigan Department of Treasury*, a Keweenaw Bay Indian Community member challenged Michigan's imposition of its use tax on a vehicle purchased out of state, garaged by the member within the boundaries of the Reservation, and used on and off Reservation for personal and business travel. Mich. Tax Tribunal Dkt. No. 283437 (Apr. 20, 2005). The Tribunal applied *Moe*, *Colville*, and *Sac & Fox* to confirm that Michigan could only tax off-Reservation of property of a tribe or tribal member "if the tax applied exclusively to off-

reservation use within the state," and that an "unapportioned tax that included 'on- and off-' reservation use was identical to a direct tax on the tribal member." *Id.* at 4. In finding Michigan's imposition of the use tax unlawful, the Tribunal expressly rejected the State's argument that "the amount of off-reservation use of the subject vehicle" was relevant to the lawfulness of the use tax as applied, and found that "off-Reservation use is irrelevant" because the use tax "is not specifically designed and explicitly stated as tailored to specific use on and off-reservation." *Id*.

Based on *Moe* and its progeny, and as the Michigan Tax Tribunal has recognized in *Chosa*, a state is without power to impose a tax upon property principally housed, garaged, and stored by an Indian tribe or tribal member within Indian country and used within and outside Indian country unless the taxing statute provides a mechanism for apportioning the tax to exclude the activity within Indian country.

ARGUMENT

I. DEFENDANTS HAVE VIOLATED FEDERAL LAW BY IMPOSING SALES TAX UPON RETAILERS FOR THE SALE, LEASE OR RENTAL OF PROPERTY TO THE COMMUNITY OR ITS MEMBERS WITHIN THE RESERVATION.

The Indian Trader Statutes categorically bar a state from imposing a tax on an Indian trader for sales to Indians within their Indian country. For purposes of applying this federal immunity, vendors making sales to Indians within their Indian country qualify as Indian traders regardless of whether the vendors have Indian trader licenses or places of business within Indian country. This immunity applies to all sales made to an Indian tribe or Indian within their Indian country, regardless of the nature or use of the property sold. Under black letter federal law, states simply cannot tax such transactions.

Because the legal incidence of the Michigan sales tax falls upon the retailer, Defendants

are categorically barred from imposing the tax upon retailers for sales of property to the Community or its members within the Reservation.

A. Federal Law Preempts the Michigan Sales Tax Because it Falls Directly on Indian Traders.

Michigan sales tax is imposed directly on the retailer for the privilege of engaging in the retail sale of tangible personal property or services and the retailer bears the legal incidence of the tax. *See*, *e.g.*, Mich. Att'y Gen. Op. No. 7062 (Oct. 4, 2000); *Sims v. Firestone Tire & Rubber Co.*, 397 Mich. 469, 473, 245 N.W.2d 13 (1976); *Fed. Res. Bank of Chicago v. Dep't of Revenue*, 339 Mich. 587, 591, 64 N.W.2d 639 (1954); *Nat'l Bank of Detroit v. Dep't of Revenue*, 334 Mich. 132, 138, 54 N.W.2d 278 (1952). The Department expressly concedes this point in the boilerplate language in its Exemplar Claim denial letters. *E.g.*, Nichols Decl. Ex. 9 (6-12-2015 Claim) at SOM-FED00009285. Liability for the tax is triggered in any given instance when the vendor makes a "sale at retail" that is not otherwise exempt under the statute. Mich. Comp. Laws §§ 205.51(1)(b), 205.52(1). Pursuant to *Central Machinery*, retailers making sales of tangible personal property or services to the Community or its members within the Reservation constitute Indian traders for purposes of federal preemption analysis—even if the retailer does not have a place of business on the Reservation and is not licensed as an Indian trader. 448 U.S. at 164-65. Accordingly, under black letter federal law, Defendants are categorically barred from imposing Michigan sales tax on retailers for sales of tangible personal property to the Community or its members within the Reservation

Thumbing their nose at the Indian Trader precedents, Defendants have peremptorily denied refunds in at least 1,185 instances where the Community or a member made purchases within the Reservation, and specifically has denied *all* sales tax refund claims submitted by Community members. Nichols Decl. Ex. 1 (Summary Chart). Three representative samples of

these 1,185 instances include:

- *Denial of Community Member claim arising from a 2012 online purchase of a sauté pan and a child's toy from Walmart.com for delivery within the Reservation*. Nichols Decl. Ex. 13 (11-18-2012 Claim) at SOM-FED00012335-39. Because this sale took place on the Reservation under Michigan sales tax law, Mich. Comp. Laws § 205.69(1), the Community Member applied for a sales tax refund of $7.38. Nichols Decl. Ex. 13 (11-18-2012 Claim) at SOM-FED00012337-38. The Department denied the claim on grounds that the transaction "may not have" taken place in Indian country and "after balancing all interests, it is clear that the State's interests are sufficient to justify its tax." *Id*. (11-18-2012 Claim) at SOM-FED00012336.
- *Denial of Community claim arising from 2014 purchase of wall signs from Michigan retailer*. Nichols Decl. Ex. 19 (3-17-2014 Claim) at SOM-FED00008515-16. The Community ordered the signs from the Reservation for delivery on the Reservation. Because this sale took place on the Reservation under Michigan law, Mich. Comp. Laws § 205.69(1), the Community applied for a sales tax refund of $14.30, noting on its claim that the signs would be used in the Ojibwa Casino on the Reservation. Nichols Decl. Ex. 19 (3-17-2014 Claim) at SOM-FED00008517-19. The Department denied the claim on grounds that "after balancing all interests, it is clear that the State's interests are sufficient to justify its tax." *Id*. (3-17-2014 Claim) at SOM-FED00008515.
- *Denial of Community claim arising from 2014 purchase of electrical parts from Michigan retailer, for use in the Ojibwa Hotel*. The Community made the

> purchase from the Reservation and the parts were delivered to the Reservation. Because the sale took place on the Reservation under Michigan law, Mich. Comp. Laws § 205.69(1), the Community applied for a sales tax refund of $12.81, noting that the parts would be used in the Ojibwa Hotel on the Reservation. Nichols Decl. Ex. 10 (7-2-2014 Claim) at SOM-FED00009327-28. The Department denied the claim on grounds that "after balancing all interests, it is clear that the State's interests are sufficient to justify its tax." *Id*. (7-2-2014 Claim) at SOM-FED00009325.

The Department's excuse for denying these claims is presumably its conclusion that the purchases were not made for use in what the Department views to be an "essential government function." Nichols Decl. Ex. 6 (Defs.' Disc. Resp.) at Resp. Interrog. No. 1. This "essential governmental function" consideration, however, has no basis whatsoever in the federal Indian Trader exemption authorities. Both *Warren Trading* and *Central Machinery* concerned sales of items that had *no conceivable connection* to an "essential governmental function, but rather consisted of daily necessities (food, clothing, etc.) and equipment for business operations on the reservation.[11] Not only is the "essential governmental function" irrelevant and unsupported by federal Indian law, it is applied by Defendants in an arbitrary and inconsistent manner. For example, the Department granted a refund request for a vehicle purchase by the Community's Public Works Department, but refused to acknowledge that a "Tribal Center Government Vehicle" supports an "essential government function." *See* Nichols Decl. Exs. 28 (4-17-2015

[11] *See* Oral Argument at 0:31:31-49; 49:17-50:25, *Warren Trading Post Co. v. Ariz. Tax Comm'n*, 380 U.S. 685 (No. 115), https://www.oyez.org/cases/1964/115; Oral Argument at 0:00:40-54, *Cent. Mach. Co. v. Ariz. State Tax Comm'n*, 448 U.S. 160 (No. 78-1604), https://www.oyez.org/cases/1979/78-1604.

Claim) at 8, and 29 (4-27-2016 Claim) at 8 (questioning the function of the Tribal Government Center).

The 1,206 denied claims are just a small representative sample of the hundreds of thousands of other transactions for which refund applications were not submitted because the Community and its members lack the time and resources to challenge the application of the sales tax to every individual transaction. *See* Swartz Decl. ¶ 12.

B. Federal Law Preempts Application of the Use Tax on Lessors to the Community or Members Because the Tax Falls Directly on Indian Traders.

Generally, the legal incidence of the Michigan use tax falls on the consumer of products and services sold at retail; however, lessors may purchase property free of sales tax if they elect to pay use tax on the rental receipts instead. *See* Mich. Comp. Laws § 205.93(1); Mich. Dep't of Treasury, Revenue Admin. Bulletin No. 2015-25, at 5 (Dec. 2, 2015) (courtesy copy included as Addendum B to Nichols Declaration). Pursuant to the principles of *Central Machinery*, lessors—just like retail sellers—of tangible personal property to the Community or its members within the Reservation are Indian traders for purposes of federal preemption analysis. 448 U.S. at 164-65; 25 C.F.R. § 140.5(a)(6) ("Trading," as defined for purposes of the Indian Trader Statutes, "means buying, selling, bartering, renting, *leasing*, permitting and any other transaction involving the acquisition of property or services.") (emphasis added). Accordingly, Defendants are categorically barred from imposing the Michigan use tax against a lessor on lease payments from the Community or its members for property leased and used within the Reservation.

Defendants' responses to the Exemplar Claims show that Defendants are in fact imposing the use tax unlawfully. For example, the Community's Ojibwa Casino (located on the Reservation) leases dishwashing machines from Ecolab, and Ecolab assesses the Michigan use tax of $7.38 on each payment. *E.g.*, Nichols Decl. Ex. 15 (5-19-2015 Claim) at SOM-

FED00008787-88. The Community sought refunds of these tax payments, and the Department denied them on the grounds that "[w]hile the Tribe's use of the item(s) may not be subject to the Michigan use tax, the lessor's use is" and "the use tax submitted by the lessor is due and the Tribe's refund request is denied." *Id*. (5-19-2015 Claim) at SOM-FED00008783; *see also* Nichols Decl. Ex. 20 (2-20-2014 Claim) at SOM-FED00009383 (rejection of refund on property leased from Aramark). The Department claims to have informed Ecolab "that the Tribe is exempt in this situation, however, use tax is still due from the lessor." Nichols Decl. Ex. 15 (5-19-2015 Claim) at SOM-FED00008783. The Department contends that whether "the lessor chooses to pass on the expense is a matter between the lessor and the Tribe." *Id*. (5-19-2015 Claim). Defendants treat the Community's other lease payments in the same manner. *See*, Nichols Decl. Ex. 1 (Summary Chart) at lines 231-234, 262-264, 318-322 (Aramark leases); *e.g.*, Ex. 20 (2-20-2014 Claim) at SOM-FED00009383.

By insisting that the lessors pay use tax on leases of equipment to the Community or its members for use on the Reservation, the Department directly violates the holdings in *Warren Trading*, *Central Machinery*, and *Milhelm Attea*. These cases categorically bar states from imposing a tax on retailers (Indian traders) with respect to sales to Reservation Indians, and the Michigan use tax in these circumstances is directly imposed on the retailers. Imposition of the use tax on lessors in these circumstances, in fact, flatly violates Michigan state law, which precludes application of the use tax to a lessor if the lessee (or the lessee's use) is exempt from the use tax. Mich. Dep't of Treasury, Revenue Admin. Bulletin No. 2015-25, at 5 (Dec. 2, 2015) ("If the lessee of the property is an entity that is exempt from tax under the Use Tax Act or the property itself is exempt from use tax then the lessor is not liable for use tax on the rental receipts.") Here, the Department apparently concedes that the Community's use of leased

property in its Indian country is exempt from the use tax, but collects the tax anyway. *See*, *e.g.*, Nichols Decl. Ex. 15 (5-19-2015 Claim) at SOM-FED00008783.

C. Defendants Cannot Rely on a Balancing of Interests Analysis to Justify a Tax Otherwise Preempted Under Federal Law.

Defendants have not addressed the Indian Trader Statutes, *Warren Trading*, or *Central Machinery* at all in their rejection of those Exemplar Claims regarding sales on the Reservation. *See, e.g.*, Nichols Decl. Ex. 11 (3-10-2016 Claim) at SOM-FED00009189. Instead, Defendants rely on their interpretation of the balancing of interests test articulated in *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980), and contend that "the State's interests are sufficient to justify its tax." Nichols Decl. Ex. 11 (3-10-2016 Claim) at SOM-FED00009189. But the law is clear: Defendants cannot rely on the *Bracker* balancing test to justify a tax that is categorically preempted under federal law on other grounds.

In *Bracker*, the Supreme Court started from the premise that the *Warren Trading* holding—as affirmed in *Central Machinery*—regarding the preemptive effect of the Indian Traders Statutes was settled law. 448 U.S. at 144, 151. *Bracker* did not disturb the holdings in *Warren Trading* or *Central Machinery*; in fact, it used the *Warren Trading* framework—which established the preemptive effect of the Indian Trader Statutes—as a model for evaluating the preemptive effect of *other* federal regulatory schemes. 448 U.S. at 152-53. Thus, *Bracker* is not a mechanism for justifying the imposition of a state tax where it is otherwise preempted by federal law. To the contrary, *Bracker* balancing *broadens* the scope of federal preemption of state jurisdiction over Indians so that such preemption "is not limited to those situations where Congress has explicitly announced an intention to pre-empt state activity," as it did with the Indian Trader Statutes. *Ramah Navajo Sch. Bd. v. Bureau of Revenue of New Mexico*, 458 U.S. 832, 838 (1982) (citing *Bracker*, 448 U.S. at 143-44). *Central Machinery* and *Bracker* were

issued on the very same day, June 27, 1980, and the Court was obviously aware of the analysis in each decision (indeed, *Central Machinery* includes a citation to *Bracker*). *Bracker*, 448 U.S. at 136; *Central Machinery*, 448 U.S. at 160, 170. If *Bracker* balancing were relevant to the legality of the taxation of Indian traders making sales or leases to Indians within Indian country, the Court would have applied that balancing of interests analysis in *Central Machinery*. The Court did not do so because it concluded that *Warren Trading* had resolved the preemption analysis with respect to Indian traders, and thus state taxation of transactions between Indian traders and Indian tribes and tribal members were categorically preempted. 448 U.S. at 165-66.

The United States Supreme Court, in short, did all the preemption analysis in *Warren Trading* —balancing or otherwise—that it deemed necessary with respect to state taxation of Indian traders, and having done so, categorically barred the imposition of direct taxes on retailers making sales to reservation Indians within their reservation. No further balancing by the Department or this Court is warranted, and the Department's purported application of *Bracker* balancing to the sales at issue here has absolutely no basis in federal Indian law.

III. DEFENDANTS HAVE VIOLATED FEDERAL LAW WITH RESPECT TO THEIR IMPOSITION OF THE MICHIGAN USE TAX ON PROPERTY PRINCIPALLY HOUSED, STORED OR GARAGED WITHIN THE RESERVATION.

The Supreme Court has repeatedly held that a state is categorically barred from imposing a tax upon Indians for activities or transactions that take place within Indian country. *See infra* Standard of Decision, Part II.B, *supra.* The Michigan Tax Tribunal in *Chosa* has held, based on this authority, that Michigan cannot impose its use tax on property owned by a Community member and stored on the Reservation, even if the Community member uses the property outside the Reservation. MTT Dkt. No. 283437 at 4. Because the Use Tax Act does not apportion the use tax by statute to the amount of actual off-reservation use, the Tax Tribunal correctly held that

the use tax could not apply at all to property principally housed, stored or garaged within the Reservation, regardless of whether the property is also used off the Reservation. *Id*.

The Use Tax Act has not changed in any material respect since *Chosa* was decided. The use tax is imposed upon a person for the privilege of using, storing, or consuming within Michigan tangible personal property upon which the Michigan sales tax has not been paid and which is not otherwise exempt. Mich. Comp. Laws § 205.93(1). The legal incidence of the use tax falls upon the user of the tangible personal property or services and the trigger of the tax is the use, storage, or consumption of such property or services. *Id.* As the Michigan Tax Tribunal recognized in *Chosa*, the Use Tax Act has no apportionment formula that would tailor it to the amount of actual use of tangible personal property outside the Reservation. Indeed, Defendants admit—as they must—that the "Use Tax Act does not provide a mechanism that tailors or apportions the use tax so that it is calculated based solely on the percentage of use outside the Community's Indian country." Nichols Decl. Ex. 6 (Defs.' Disc. Resp.) at Req. for Admission No. 8.

Nevertheless, despite clear Supreme Court precedent on this topic, and the clear application of this precedent by the Michigan Tax Tribunal Defendants continue to collect the use tax, and have denied refunds in at least three instances – two involving vehicles and one involving clothing – where the Community or a member used, stored, or consumed tangible personal property or services within the Reservation and trust lands. For example, the Department denied in 2013 the $60.00 refund request for a Community Member's purchase of a used Toyota truck which the Member certified on the claim would be garaged on the Reservation and used on and off the Reservation. Nichols Decl. Ex. 14 (12-10-2012 Claim) at SOM-FED00011473.

Under the longstanding federal law reaffirmed in *Chickasaw Nation*, *Moe*, *Colville*, and *Sac & Fox Nation*, Defendants are absolutely precluded from imposing the Michigan use tax upon the Community or its members with respect to their use, storage, or consumption of tangible personal property or services within the Reservation—regardless of whether it is also used outside of the Reservation.

IV. DEFENDANTS HAVE IMPROPERLY DENIED OR FAILED TO ACT ON CLAIMS SUBSTANTIALLY IDENTICAL TO CLAIMS THEY HAVE GRANTED.

As noted above, Defendants have denied or failed to act on a number of claims substantially identical to claims they have granted. *See* Undisputed Facts, Part IV.C.3, *supra* (addressing Nichols Decl. Ex. 1 (Summary Chart)). These claims—including at least the claims for purchases from Quill.com that were denied and the three claims for purchases from American Hotel Register that have not been decided—should have been granted for the additional reason that other substantially identical claims have been granted.

V. THE REFUND AND EXEMPTION PROCESS IMPOSES UNLAWFUL BURDENS ON THE COMMUNITY'S AND COMMUNITY MEMBERS' EXERCISE OF THEIR FEDERAL LAW TAX IMMUNITIES.

Under clear and longstanding precedents, Defendants are categorically barred from imposing Michigan's sales and use taxes on sales and leases to the Community and its members on the Reservation. Because the federal exemptions are simple and categorical, Defendants have no basis for requiring the Community and its members to participate in its burdensome Refund and Exemption Process. This Process forces the Community and its members to pay the tax, file documentation and refund forms for each purchase, and wait weeks or sometimes months for the Department's response. *See* Undisputed Facts, Part IV.A, *supra.* The Department evaluates the refund claims based on irrelevant and inapplicable legal criteria and rejects over 90% of the claims. *See* Nichols Decl. Ex. 1 (Summary Chart). Moreover, the Department issues approvals

and checks in a manner that makes it virtually impossible to determine whether the Department actually pays all of the refunds that it approves. Nichols Decl. Ex. 28 (4-17-2015 Claim) at 9 (remittance advice) Swartz Decl. ¶ 11.

The Department's Refund and Exemption Process not only burdens and discourages the Community and its Members from exercising a categorical federal exemption, it violates the Community and its members' rights to due process and equal protection, as guaranteed by the Fourteenth Amendment to the U.S. Constitution, because the Community and its members are treated "disparately as compared to similarly situated persons" and "such disparate treatment . . . targets a suspect class." *Ctr. for Bio-Ethical Reform, Inc. v. Napolitano*, 648 F.3d 365, 379 (6th Cir. 2011) (quoting *Club Italia Soccer & Sports Org., Inc. v. Charter Twp. of Shelby, Mich.*, 470 F.3d 286, 299 (6th Cir. 2006)). State action using a racial classification may be upheld "only if it is necessary, and not merely rationally related, to the accomplishment of a permissible state policy." *McLaughlin v. Florida*, 379 U.S. 184, 196 (1964). "[A]ny official action that treats a person differently on account of his race or ethnic origin is inherently suspect," *Fullilove v. Klutznick*, 448 U.S. 448, 523 (1980) (Stewart, J. dissenting), and in nearly all circumstances, the use of a suspect racial classification "has proven automatically fatal" to government defenses. *Missouri v. Jenkins*, 515 U.S. 70, 121 (1995).

Defendants, as state officials and agents, impose dramatically greater burdens on the Community and its members than on non-Indian persons or entities that claim exemptions or immunity from sales or use taxes. Churches, 501(c)(3) and other tax-exempt organizations, retailers, and other entities have tax exemptions that can be exercised simply by completing a form and presenting it to the seller—these entities bear no burden that even comes close to the Refund and Exemption Process that applies to the Community. Nichols Decl. Ex. 5 (Form

3372). The Community and its members are singled out for this disparate treatment because they are Indians—the Refund and Exemption Process applies to no other class of person—and this suspect racial classification[12] is subject to the strictest scrutiny; it may be upheld "only if it is necessary, and not merely rationally related, to the accomplishment of a permissible state policy." *McLaughlin*, 379 U.S. at 184. As shown below, Defendants cannot show that the Refund and Exemption Process is necessary to the accomplishment of any legitimate state policy.

There is no dispute that the Community and its members are treated differently, and worse, than other tax-exempt or immune entities and people. For example, 501(c)(3) and

[12] "[A]ll racial classifications reviewable under the Equal Protection Clause must be strictly scrutinized." *Gratz v. Bollinger*, 539 U.S. 244, 270 (2003) (*quoting Adarand Constructors, Inc. v. Pena*, 515 U.S. 200, 224 (1995)). Thus, "any person, of whatever race, has the right to demand that any governmental actor subject to the Constitution justify any racial classification subjecting that person to unequal treatment under the strictest of judicial scrutiny." *Id.* Defendants cannot justify their use of a racial classification here by relying on cases that applied rational basis scrutiny to some Indian classifications because those cases addressed laws enacted by the federal government that could "be tied rationally to the fulfillment of Congress' unique obligation toward the Indians." *Morton v. Mancari*, 417 U.S. 535, 555 (1974). For such classifications, "ordinary rational basis scrutiny applies to Indian classifications just as it does to other non-suspect classifications under equal protection analysis." *Narragansett Indian Tribe v. National Indian Gaming Commission*, 158 F.3d 1335, 1340 (D.C. Cir. 1998). In contrast, state classifications—especially those that operate to the detriment, rather than the benefit, of Indians—are not entitled to the same deference. *See Washington v. Confederated Bands & Tribes of Yakima Indian Nation*, 439 U.S. 463 (1979) ("It is settled that the unique legal status of Indian tribes under federal law permits the Federal Government to enact legislation singling out tribal Indians, legislation that might otherwise be constitutionally offensive. States do not enjoy this same unique relationship with Indians . . . .") (internal citations omitted). As the First Circuit recently noted, *Mancari* "relied on several sources of federal authority to reach its holding, including the portion of the Commerce Clause relating to Indian tribes, the treaty power, and the special trust relationship between Indian tribes and the federal government," however, "the states have no such equivalent authority, which is ceded by the Constitution to the federal government." *K.G. Urban Enterprises, LLC v. Patrick*, 693 F.3d 1, 19 (1st Cir. 2012). Defendants cannot rely on any constitutional provision, trust obligation, treaty, or other authority to justify their disparate treatment of the Community and its members with respect to the exercise of tax immunities. Accordingly, strict scrutiny must be applied to the racial classification at issue here.

501(c)(4) organizations, retailers, industrial processors, churches, hospitals, schools, and government purchasers (other than the Community) can exercise their tax immunity or exemption by simply filling out Department Form 3372, "Michigan Sales and Use Tax Certificate of Exemption," and providing a copy to the seller; the purchaser does not need to produce any additional documentation. Nichols Decl. Ex. 5 (Form 3372). Upon doing so, the seller will not be required to pay the sales tax or collect the use tax from the purchaser as long as the seller receives and accepts the Form 3372 in good faith. *Id*. (Form 3372). The certificate may apply to a single transaction, but also may be designated as a "Blanket Certificate" (with a default term of four years) for recurring business relationships. *Id*. (Form 3372). Wholesalers are not even required to use Form 3372 to exercise their exemption—they may simply provide a written statement that they are purchasing for "resale at wholesale." *Id*. (Form 3372). The process for exercising these immunities and exemptions is administered by the purchasers and sellers, with no requirement to pay the sales or use tax and then prepare and file a refund claim with the Department or to wait to obtain the Department's advance approval of the immunity or exemption before undertaking the purchase and sale. *Id*. (Form 3372). In contrast, the Community and its members are required to apply for an exemption or refund for every transaction in which they engage.[13] As explained above, the Refund and Exemption Process is so burdensome that it effectively prevents the Community and its members from exercising their federal law tax immunities—and this would true even if Defendants were correctly applying the law to the requests for refunds and exemptions. *See* Swartz Decl. ¶ 12; S. LaFernier Decl. ¶ 6; M. LaFernier Decl. ¶ 6; E. Mayo Decl. ¶ 6; S. Mayo Decl. ¶ 6.

[13] While the application form for tribes provides a box for the tribe to indicate whether a purchase of specific property for a specific purpose is intended to be recurring, the application form for tribal members contains no similar box.

To the Community's knowledge, no other state uses a process that imposes even a tiny fraction of the burdens imposed by Defendants' Refund and Exemption Process. Indeed, in many states, tribes and tribal members may use exemption certificates very similar to Michigan's Form 3372 to exercise their federal tax immunities. *See, e.g.*, Nichols Decl. Addenda C (Arizona Form), D (Idaho Form); E (New York Form); F (Washington Form); and G (Wisconsin Form).

Defendants' justifications for the Department's unprecedented Refund and Exemption Process are spurious. Defendants claim that the applicability of the Community's and its members' tax immunities must be analyzed with respect to the specific circumstances of each transaction, and that the Community and its members cannot be trusted, apparently because of their race or ethnicity, to exercise their immunities without supervision of Defendants. Nichols Decl. Ex. 31 (W. Fratzke Ltr. Nov. 14, 2013) ("[A] point of sale exemption process without appropriate safeguards is not something the State is comfortable with"). These purported justifications are not adequate to meet Defendants' heavy burden of showing that the process is "necessary . . . to the accomplishment of a permissible state policy." *McLaughlin*, 379 U.S. at 196. There is no need for the Department to act as a gatekeeper of the Community's and its members' exercise of their immunities because, as explained above, the immunities apply under readily ascertainable and verifiable circumstances: (1) the purchaser or consumer is the Community or a Community member; and (2) the transaction occurs in Indian country, or the purchased good or service is principally located in Indian country. *See* Argument Parts I and II, *supra*. Community or member status can be verified with tribal identification documents. Swartz Decl. ¶ 4; Ex. A (Member ID). The Community's Indian country is a defined area with borders established by law and ascertainable from publicly available sources. *Id*. ¶¶ 5-6; Exs. B (Reservation Map), C (Trust Deed). And because the conditions for claiming the immunity are

so readily determined, any attempt to fraudulently exercise the immunities would also be obvious. *See id*. The Refund and Exemption Process does not advance any state interest in verifying the application of Indian tax immunity or deterring fraud, it only imposes unnecessary burdens on the Community and its members and prevents them from exercising their federal rights. For this reason, the Defendants' Refund and Exemption Process violates the Community's and its members' rights to equal protection of the laws.

CONCLUSION

For the foregoing reasons, the Community respectfully requests that this Court enter partial summary judgment for the Community providing, at a minimum, the following relief:

1. A declaration that the Michigan sales and use taxes are invalid as applied to (a) the purchase, lease, rental, use, storage, or consumption of tangible personal property or services by the Community and its members within the Community's reservation and trust lands, and (b) the use, storage, or consumption of tangible personal property by the Community or its members that is used or consumed both within and outside the reservation or trust lands but is principally housed, stored, or garaged within the reservation or trust lands;

2. A declaration that with respect to any sale, lease, rental, use, storage, or consumption of tangible personal property or services within the Community's reservation and trust lands, the seller is entitled to rely on a single use or a blanket certificate of federal tax immunity provided by the purchaser containing information and a certification similar to that required in the Michigan Department of Treasury Form 3372, entitled "Michigan Sales and Use Tax Certificate of Exemption," stating that the purchaser is the Community (including any of its departments or enterprises) or a Community member, and shall not be liable for any Michigan sales or use tax if the purchaser improperly claims an exemption, unless the seller has committed fraud or has solicited the purchaser to make an improper claim of federal tax immunity;

3. An order enjoining Defendants from enforcing the Michigan Sales and Use Tax Acts against the Community, its members, or any seller to the Community or its members with respect to (a) the purchase, lease, rental, use, storage, or consumption of tangible personal property or services by the Community and its members within the reservation and trust lands, and (b) the use, storage, or consumption of tangible personal property by the Community or its members that is used or consumed both within and without the reservation or trust lands but is principally housed, stored, or garaged within the reservation or trust lands;

4. An order requiring Defendants to:

(a) Mail notices to all retail sellers and lessors located in Baraga, Houghton, and Marquette Counties that currently hold a Michigan sales tax license with the following text:

> The Michigan sales tax does not apply to the purchase, lease, or rental of tangible personal property or services by the Keweenaw Bay Indian Community and its Members within the Community's reservation and trust lands. This rule applies to any transaction in which the purchased property is delivered to the Community or its Members on the Community's reservation or trust lands.
>
> Starting immediately, you may rely on the purchaser's presentation of a tribal identification, or written certification that the purchaser is the Community (including all departments and enterprises of the Community) or a Community Member, and that the delivery address is on the Community's reservation or trust lands; upon acknowledging such documentation in good faith, you will not be required to pay the sales tax. This procedure will remain in place until such time as the Department may issue a Michigan Sales and Use Tax Certificate of Exemption applicable to purchases by the Community and its Members.

(b) Mail notices to such retail sellers and lessors as the Community may identify with the following text:

> The Michigan use tax does not apply to the use, storage, or consumption of tangible personal property by the Keweenaw Bay Indian Community or its Members if such property is principally housed, stored, or garaged within the Community's reservation or trust lands, even if the property may be used or consumed both

> within and outside the reservation or trust lands.
>
> The Michigan use tax also does not apply to lessors that lease tangible personal property to the Keweenaw Bay Indian Community or its Members if such property is principally housed, stored, or garaged within the Community's reservation or trust lands, even if the property may be used or consumed both within and outside the reservation or trust lands.
>
> Starting immediately, you may rely on the purchaser's presentation of a tribal identification, or written certification that the purchaser is the Community (including all departments and enterprises of the Community) or a Community Member, and that the purchased property will be principally housed, stored, or garaged within the Community's reservation or trust lands; upon acknowledging such documentation in good faith, you will not be required to collect the use tax from the purchaser, or pay the use tax with respect to leased property. This procedure will remain in place until such time as the Department may issue a Michigan Sales and Use Tax Certificate of Exemption applicable to purchases by the Community and its Members.[14]

(c) Post on the Department of Treasury's website, at a location conspicuous on, and readily accessible from, the Sales and Use Tax homepage (http://www.michigan.gov/taxes/0,4676,7-238-43519_43529---,00.html), the text set forth in (a) and (b) above.

5. An order enjoining Defendants from (a) providing information or instructions to sellers to the Community or its members that is inconsistent with the declarations sought in paragraphs 1 and 2 above, (b) imposing a system requiring pre-approval from Defendant Fratzke, the Department, or any other Michigan agency or official for any purchase, lease, rental, use,

[14] This Court has the authority to order defendants to post or disseminate notices regarding the Court's decision. *See, e.g., United States v. Zen Magnets, LLC*, 170 F. Supp. 3d 1365, 1380 (D. Colo. 2016) (ordering defendant to post notice of court's order on website and all social media accounts); *Hare v. Potter*, 549 F. Supp. 2d 688, 698 (E.D. Pa. 2007) (ordering Defendants to post notice of verdict in regional offices).

storage, or consumption of tangible personal property or services that falls within the facts described in the declaration sought in paragraph 1 above or that is accompanied by a certificate of federal tax immunity provided by the purchaser to the seller that meets the requirements set forth in the declaration sought in paragraph 2 above, or (c) imposing a recordkeeping system on sellers with respect to any facts beyond those described in the declaration sought in paragraph 1 above; and

6. An order awarding the Community such other relief as the Court deems just and appropriate.

Dated: November 9, 2017

Respectfully submitted,

DORSEY & WHITNEY LLP

By _s/James K. Nichols_____
Skip Durocher (MN Bar No. 208966)
Mary J. Streitz (MN Bar No. 016186X)
James K. Nichols (MN Bar No. 0388096)
Suite 1500
50 South Sixth Street
Minneapolis, MN 55402
Tel: (612) 340-7855
Fax: (612) 340-2807

Attorneys for Plaintiff the Keweenaw Bay Indian Community

Danielle Webb (MI Bar No. P77671)
Tribal Attorney's Office
Keweenaw Bay Indian Community
16429 Beartown Road
Baraga, Michigan 49908
Telephone: (906) 353-4107
Fax: (906) 353-7174