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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1. In light of the strong interests of the Keweenaw Bay Indian Community ("the Community") and the federal government in ensuring and providing for the Community's self-government, self-determination, self-sufficiency, and economic development—and the corresponding lack of any legitimate State interest—may Defendants impose the Michigan Sales Tax with respect to purchases made by the Community and its members on the Community's Reservation and trust lands?

Most Apposite Authority:

Ramah Navajo Sch. Bd. v. Bureau of Revenue of New Mexico, 458 U.S. 832 (1982)

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2. In light of the strong interests of the Community and the federal government in ensuring and providing for the Community's self-government, self-determination, self-sufficiency, and economic development—and the corresponding lack of any legitimate State interest—may Defendants impose the Michigan Tobacco Tax, and other requirements of the Tobacco Products Tax Act, with respect to the Community's purchase and resale of tobacco on Reservation and trust lands, and the Community employees involved in such purchase and resale?

Most Apposite Authority:

Ramah Navajo Sch. Bd. v. Bureau of Revenue of New Mexico, 458 U.S. 832 (1982)

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3. In light of the well-established law regarding Indian tribes' rights of self-government and sovereignty, may Defendants impose the Michigan Sales Tax with respect to purchases made by the Community and its members on the Community's Reservation and trust lands?

Most Apposite Authority:

Washington v. Confederated Tribes of the Colville Indian Reservation, 447 U.S. 134 (1980)

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4. In light of the well-established law regarding Indian tribes' rights of self-government and sovereignty, may Defendants impose the Michigan Tobacco Tax, and other requirements of the Tobacco Products Tax Act, with respect to the Community's purchase and resale of tobacco on Reservation and trust lands, and the Community employees involved in such purchase and resale?

Most Apposite Authority:

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5. In light of the well-established law regarding Indian tribes' rights of self-government and sovereignty, may Defendants engage in law enforcement operations in the Community's Indian country for the purpose of enforcing state law, or investigating suspected violations of state law?

Most Apposite Authority:

Williams v. Lee, 358 U.S. 217 (1959)

Rodewald v. Kan. Dep't Revenue, 297 P.3d 281 (Kan. 2013)

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State v. Cummings, 679 N.W.2d 484 (S.D. 2004)

6. In light of the provision in Article II of the Treaty of 1842 that, in the Ceded Area (as defined in Article I of the Treaty), "the laws of the United States shall be continued in force, in respect to [the Community and its members'] trade and intercourse with the whites, until otherwise ordered by Congress," are Defendants preempted by federal law from enforcing Michigan tax laws on commercial transactions by the Community and its members with non-Indians within the Ceded Area?

Most Apposite Authority:

Treaty with the Chippewa at La Pointe, Oct. 4, 1842, 7 Stat. 591

Ramah Navajo Sch. Bd. v. Bureau of Revenue of New Mexico, 458 U.S. 832 (1982)

White Mountain Apache Tribe v. Bracker, 448 U.S. 136 (1980)

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)

INTRODUCTION

On November 9, 2017, the Keweenaw Bay Indian Community (the "Community") filed a Motion for Partial Summary Judgment (ECF No. 125). The Community argued that it and its members enjoy absolute immunity from Michigan Sales and Use Taxes with respect to their purchase or use of personal property and services within the Community's Indian country. That motion is fully briefed and pending, and if the Community prevails on that motion, all claims relating to imposition of the Michigan Sales and Use Tax in Indian country will be resolved.

In the present motion, the Community presents an additional independent argument that Defendants cannot impose the Michigan Sales Tax on transactions involving the Community and its members: the Community and federal interests in self-governance, self-determination, and economic development outweigh the state of Michigan's interest in collecting the Sales Tax. This same balancing test precludes the Defendants from imposing the state Tobacco Tax on the Community's sale of tobacco on its Reservation and trust lands. Further, the Community's rights of sovereignty and self-governance are independent barriers to imposition of the Michigan sales, use, and tobacco taxes. Finally, the Community's long-established Treaty rights extend these tax immunities beyond the confines of the modern Reservation to all lands ceded by the Community predecessors-in-interest pursuant to the 1842 Treaty of La Pointe (the "Ceded Area"); pursuant to the plain language of that Treaty, those lands are to be treated as Indian country for purposes of trade by the Community and its members.

The State of Michigan, through Defendants, acting in their official capacities, have systematically deprived the Community and members of their federal immunities. Accordingly, this Court should enter partial summary judgment in favor of the Community on Counts II and III (unless rendered moot by a decision on the Nov. 9 motion), IV, VI, and IX-XIV of the Third Amended Complaint, holding that federal law prohibits enforcement of the Michigan Sales, Use,

and Tobacco Tax Acts with respect to trade by the Community and its members within the Reservation and the Ceded Area.

UNDISPUTED FACTS

I. The Community is a Federally-Recognized Tribal Government Responsible for Governing its Territory and Serving its Members.

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. § 5123. Swartz Decl. ¶ 2.[1] The Community is the successor in interest to the L'Anse and Ontonagon bands of Chippewa Indians and exercises 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 Reservations in the Upper Peninsula of Michigan (collectively, the "Reservation"). *Id*. The L'Anse and Ontonagon Reservations and these trust lands constitute "Indian country" within the meaning of 18 U.S.C. § 1151. The Community has approximately 3,622 enrolled members, approximately 1,040 of whom live on the Reservation. *Id*. ¶ 3.

Although the Community has made some progress in its battle against the poverty and other problems that historically afflict American Indians, there is still much work to do—Community members living on the Reservation have lower median income and higher poverty rates than other Michigan residents; for example, 20% of the members have income below the

[1] For this Motion, the Community relies upon the Second 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.

poverty level, as opposed to less than 15% of Michigan's total population. *Id.* ¶ 4; Nichols Decl. Ex. 2 (Henson Rpt. Fig. 9 and 10) (summarizing Census data).

II. The Community's Government Provides Programs and Services on the Reservation and Raises Revenue by Operating Commercial Enterprises.

The Community provides a wide variety of government programs and services for its members and other Reservation residents and visitors.

A. The Community's Government Programs and Services.

The Community maintains a comprehensive framework for governance and administrative services. Swartz Decl. ¶ 5. The Tribal Council is the governing body, vested with the sovereign legislative and executive powers of the Community, and comprises 12 members elected by the Community's enrolled membership. *Id.* ¶ 5a. The Tribal Council has created numerous committees and boards to address specific aspects of governance. *Id.*

Underneath the Tribal Council is the Community's Chief Executive Officer, who is responsible for day-to-day governmental operations, managing governmental departments, budget preparation, and developing policy and procedure. *Id.* ¶ 5b. The Office of the Tribal Attorney protects the Community's legal interests and provides legal services to the Community, prosecutes crimes that occur on the Reservation, and advises the Community and its representatives in judicial, legislative, executive, and administrative proceedings. *Id.* ¶ 5c. The Enrollment Department processes applications for Tribal Enrollment, completes Blood Degree Certifications, maintains a membership log, conducts voter registration and issues Tribal membership cards. *Id.* ¶ 5e. The Realty Office provides professional real estate services to the Tribal Council, tribal members, and other Community departments, manages the Community's property on Reservation land in Baraga, Marquette, and Ontonagon counties, and applies to the federal government to take land into trust. *Id.* ¶ 5f. The Licensing and Motor Vehicles Division

provides vehicle registrations and issues licenses for hunting, camping, and fishing. The Gaming Commission regulates the Community's gaming enterprises. *Id.* ¶ 5h.

The Community's Public Works Department performs general maintenance, electrical and HVAC, carpentry, plumbing, painting, grounds keeping, and other services to protect and improve the condition of Community owned structures and assets. *Id.* ¶ 5i. The Community operates the water and sewer system in Zeba, half of the sewer system in Baraga, and a water plant in Chocolay Township. *Id.* ¶ 5j. The Department built and operates the Tribal Transfer Station, which provides waste collection transfer services to the Community and local jurisdictions. *Id.* ¶ 5k. The Community is contributing $47,000 to widen state road M-28 near the Community's Marquette casino expansion and has conducted and funded projects on County roads, including Ford Farm Road (completed in 2017 with a Community contribution exceeding $1.27 million) and Ben Road (completed in 2015 with a Community contribution of at least $200,000). Nichols Decl. Ex. 10 (Road Contrib.); Ex. 23 (Darragh Rpt.) at SOM-FED00014066.

The Community provides comprehensive health services to Indians (including members of other tribes) and descendants living in Baraga, Houghton, and Ontonagon Counties. Swartz Decl. ¶ 6. The Donald A. LaPointe Health & Education Center provides comprehensive healthcare and pharmacy services. *Id.* ¶ 6a. The New Day Treatment Facility provides substance abuse treatment and counseling, with an 18-bed capacity for residential treatment programs, as well as outpatient treatment, therapy, and recovery support services. *Id.* ¶ 6b. New Day services are available to both Community and non-Community members. *Id.*

The Community operates the Tribal Court, hears criminal, civil, family, and juvenile delinquency cases, and interprets the laws and ordinances passed by the Tribal Council. *Id.* ¶ 7. The Tribal Court employs a Chief Judge, an Associate Judge, a Chief Clerk, a Deputy Clerk, a

Probation Officer, and a Drug Court Coordinator, and provides a Public Defender to criminal defendants. *Id*. The Trial Division operates continuously, and when necessary, the Appellate Division convenes to hear and decide appeals. *Id*.

The Community provides a wide range of social services and financial assistance to members in need. *Id*. ¶ 8. The Community Assistance Program promotes the self-sufficiency of Community members by supporting quality of life, health, and welfare. *Id*. ¶ 8a. The Housing Program provides affordable, subsidized, transitional, and market-rate housing opportunities to qualifying members of the Community. *Id*. ¶ 8b. Elder and Adult Protective Services investigates allegations of abuse, neglect, or exploitation of the elderly or adults with disabilities. *Id*. ¶ 8c. The Office for Violence Against Women Program provides services to victim-survivors of domestic violence, dating violence, sexual assault, and stalking. *Id*. ¶ 8d.

The Community provides many social services for children. The Child Support Services Department helps families to establish paternity, assists with establishing, monitoring, modifying, and enforcing child support orders, and provides community education for improving the lives of children. *Id*. ¶ 8f. Child Protective Services protects child safety through positive goal oriented interventions including advocacy, education, guidance and support of families. *Id*. ¶ 8g. Foster Care Services include assessments and home studies for child foster home licensing. Social Services provides support, advocacy, and case management services for children in out-of-home care and their families. *Id*. ¶ 8h. Foster Home Licensing establishes standards and licenses foster family homes and child care institutions within Baraga, Iron, Houghton, Marquette, Ontonagon, Dickinson, Gogebic, and Keweenaw Counties. *Id*. Indian Child Welfare Act Case Services support Community children in out-of-home care and their families who reside off the Reservation. Staff may attend state court hearings, give recommendations, make

service referrals, or advocate on behalf of Community children. *Id.* ¶ 8j. Juvenile Justice Services are used to guide and support youth offenders and their caretakers through positive goal oriented interventions. *Id.*

The Natural Resources Department administers natural resource programs for the Community within the Reservation and the Ceded Area. Swartz Decl. *Id.* ¶ 9. These programs include surface water and ground water assessment and monitoring, air and radon studies, brownfield programs, wildlife and wetland management, environmental assessments, monitoring of metallic mining and exploration activity in the Lake Superior basin, participation in the protection and enhancement of Lake Superior, and fish stocking from the Community's hatchery. *Id.* The Community also maintains camping, fishing, and beach areas, and operates a marina. *Id.* In cooperation with the Bureau of Indian Affairs, the Community manages a Wildland Firefighting crew. *Id.* ¶ 10.

The Community provides educational opportunities to its members and educational support resources for members attending local schools. Swartz Decl. *Id.* ¶ 13. It also provides scholarship assistance, a summer intern program for its members in college, and funding assistance for youth to participate in extracurricular activities. *Id.* The Community operates Keweenaw Bay Ojibwa Community College, which provides academic programs, including degree programs in business administration, early childhood education, environmental science, liberal studies, and Anishinaabe studies. *Id.* The Community Library is open to the entire local community and maintains a collection of print and non-print materials to meet the research, cultural, and informational needs of the Community. *Id.* The Historic Preservation Office protects and preserves all aspects of Ojibwa culture including protecting cultural sites, artifacts, and remains. *Id.* ¶ 12.

B. The Community's Enterprises and Economic Development Efforts.

To support the Community's governmental institutions and programs, the Community operates a number of revenue-raising enterprises. *Id*. ¶ 16. Although the enterprises are commercial in nature, the net revenues are used by the Community government to fund its operations—similar to the revenue raising function of the Michigan Lottery. *Id*. The enterprises also provide employment opportunities for Community members, residents of the Reservation, and others. *Id*. The Community's largest and most important revenue-raising enterprises are the Ojibwa Casinos and Hotels in Baraga and Marquette Michigan ("the Gaming Enterprises"). *Id*. ¶ 16.a. The Community operates the Gaming Enterprises in accordance with IGRA, the 1993 Compact with the State of Michigan, and the 2001 Consent Judgment in *Keweenaw Bay Indian Community v. United States, et al.*, No. 2:94-CV-262 (W.D. Mich.). *Id*. The Gaming Enterprises are the largest of the Community's enterprises in terms of revenue generated for government services and employment opportunities for members. *Id*. The Community also operates three service station conveniences stores, Ojibwa BP, the REZ Stop, and the Pines Convenience Store, that sell gasoline, food and beverages, tobacco, and other small retail goods. *Id*. ¶ 16.b. The Community operates, or has operated in the last five years, several other enterprises, including: radio stations (WCUP Eagle Country Radio and WGLI The Rockin' Eagle Radio); the Ojibwa Recreation Area and Marina; Ojibwa Building Supply; Ojibwa Car Wash; and, Ojibwa Laundromat. *Id*. ¶ 16c.

C. Funding for Government Programs and Services.

The Community's revenue-raising enterprises provide critically important funding for its government programs and services. In fiscal year 2016, the Community's governmental budget was about [redacted] million; with [redacted] million, or 48%, of the funds coming from the Community's enterprises. Nichols Decl. Ex. 3 (Bdgt. FY15) at KBIC_TAX0000970. For fiscal

years, 2012-2015, the Community's enterprises generated between [redacted] and [redacted] million for governmental programs, accounting for as much as 66% of the Community's total government budget. *Id*. Ex. 3-7 (Bdgt. FY12-FY16).

The other principal source of funding for the Community's governmental programs is federal funding. For example, in fiscal year 2016, the federal government provided about $5 million in funding for the Community's health programs, $400,000 for the courts, and more than $750,000 for natural resources and parks, among other program funding. *Id*. Ex. 3 (Bdgt. FY16) at KBIC_TAX0000967-70. The federal government provided similar levels of funding in prior fiscal years. *See, e.g., id*. Ex. 4-5 (Bdgt. FY12, Bdgt. FY13).

D. The Community Contributes Funds to State and Local Governments.

The Community pays 8% of the net win from the Gaming Enterprises to the Michigan Economic Development Corporation ("MEDC"), which "markets Michigan as the place to do business, assists businesses in their growth strategies, and fosters the growth of vibrant communities across the state." *About MEDC* at https://www.michiganbusiness.org/about-medc/ (last accessed Oct. 18, 2018). The Community also pays 2% of the net win from the Gaming Enterprises to local units of government, including local schools, townships, and first responders. Nichols Decl. Ex. 8 at (MGCB Rpt.) at 5. In 2017, the Community contributed $549,288 to local governments and $2,197,152 to MEDC. *Id*. Since 2013, the Community has contributed more than $100,000 per year directly to public schools in Baraga and Marquette counties, with nearly $182,000 going to L'Anse Area Schools and $366,775.91 going to Baraga Area Schools over the five year period. *Id*. Ex. 9 (School Contrib.) The Community also contributes to local road projects—more than $1.5 million since 2015—and donated more than $500,000 to local charities in the last six fiscal years. Nichols Decl. Ex. 10 (Road Contrib.); Swartz Decl. ¶ 15 (charity).

III. The State, Acting Through Defendants, Imposes Sales Tax on Transactions Involving the Community and its Members in Indian Country.

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 (the "Sales Tax"). 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"). The Sales Tax Act provides for a number of exemptions from the Sales Tax, and 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 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) (hereafter, the "Sales Tax Sourcing Rule"). If the place-of-receipt rule does not apply, then the location of the sale generally is the purchaser's address. *Id*. Prior to enactment of § 205.69, unless otherwise agreed, title passes where the seller completed delivery. *World Book, Inc. v. Revenue Division*, 459 Mich. 403 (1999).

B. The Refund Process and the Claims at Issue.

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. ¶¶ 19-21; Nichols Decl. 13 (Fratzke Tr.) at at 85:6-19. As explained in the Community's pending November 9, 2017 Memorandum in Support of Motion for Partial Summary Judgment (the "Community's First SJ Memorandum"), the Department established this process following litigation that ended in 2009 but did not resolve the disputes at issue here. PageID.1608.

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.[2] Swartz Decl. ¶ 20; Nichols Decl. 13 (Fratzke Tr.) at at 85:6-19; PageID.1684 (Form 4765), PageID.1687 (Form 4766).

Since July 2012, the Community and four tribal members submitted, under protest, approximately 1,395 claims for exemption or refund to the Department ("Exemplar Claims"). Swartz Decl. ¶ 22; Nichols Decl. Ex. 1 (2018 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. ¶ 22; S. LaFernier Decl. ¶ 3; M. LaFernier Decl. ¶ 3; E. Mayo Decl. ¶ 3 ; S. Mayo Decl. ¶ 3; Mich. Comp. Laws § 205.69(1); *see also* Michigan Revenue Administrative Bulletin No. 2015-25 at 4 (Dec. 12, 2015). Of the 1,395 Exemplar Claims, the Department denied approximately 1,237 claims, granted approximately 136 claims, and has failed to rule on approximately 22 remaining claims. The denied refunds total $ 21,424.76, not including interest. Nichols Decl. Ex. 1 (2018 Summary Chart). These Exemplar Claims relate to purchase and use of a wide variety of property and services. *Id.*

[2] The Department created special forms for this process involving subject Indian tribes and tribal members. PageID. PageID.1684 (Form 4675); PageID. PageID.1687 (Form 4766).

As explained in the Community's First SJ Memorandum, the Refund and Exemption Process not only burdens the Community and its Members from exercising a categorical federal exemption, it violates their rights to due process and equal protection, as guaranteed by the Fourteenth Amendment, because they are treated "disparately as compared to similarly situated persons" and "such disparate treatment . . . targets a suspect class." PageID.1631-36. Subsequent discovery revealed additional facts supporting the Community's position. Defendant Fratzke[3] admitted that the Community and members might actually lose money through the Refund and Exemption process because the cost of postage alone might exceed the amount of the refund for many of the transactions at issue. Nichols Decl. 13 (Fratzke Tr.) at 193:4-194:6. Defendant Fratzke nevertheless confirmed that the Department is "not going to accommodate" the Community members' interests in a more efficient system. *Id*. at 197:2-14. Defendants' putative expert, tax analyst Scott Darragh, admitted that allowing the Community and members to use a point-of-sale exemption certificate presents no greater risk of fraud than already exists from the classes of tax exempt purchasers allowed to use a certificate. *Id*., Ex. 22 (Darragh Tr.) at 80: 3-8.

C. Defendants' Handling of the Refund and Exemption 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 refund applications, the Department balances all tribal, federal, and state interests based on

[3] Defendant Fratzke was the Treasury official with primary responsibility for reviewing and deciding the Exemplar Claims, and the decision letters were sent under his name. Nichols Decl. Ex. 11 (Fratzke Tr.) at 10:15-11:5, 142:21-144:6; PageID.1727. Fratzke testified that he would occasionally discuss claims with his supervisor, Mike Eschelbach. Nichols Decl. Ex. 11 (Fratzke Tr.) at 25:21-26:16; 142:3-144:13.

the circumstances of each transaction. Nichols Decl. Ex. 11 (Fratzke Tr.) at 65:14-22; 66:9-19); PageID.1704 (Resp. Interrog. No. 12). The Department claims that it designed Forms 4765 and 4766 "to solicit the information that would be necessary to do [*Bracker*] balancing." Nichols Decl. Ex. 11 (Fratzke Tr.) at 100:17-101:12. Fratzke admitted, however, that the Forms do not actually request information on tribal or federal interests relevant to the *Bracker* analysis. *Id*. at 105:9-106:7; 106:10-12.

The Department seeks to assess the location of transactions so as to "prevent the structuring of a transaction to take place in Indian Country." Nichols Decl. 14 (Pos'n Stmt.) at SOM-FED00013755. Apparently for this reason, the Department determined that the Sales Tax Sourcing Rule does not apply to determine the location of Community transactions. Nichols Decl. Ex. 11 (Fratzke Tr.) at 74:13-75:7; 76:21-77:3; 77:9-18.

At his deposition, Fratzke testified that in his evaluation of the Community and Members' Sales Tax claims "the Federal interests were taken into consideration, the State's interests were taken into consideration and the Tribe's interests were taken into consideration," and added that the decision letters do not "get into the specifics of which" interests were considered. *Id*. at 132:2-7 (discussing decision on Ojibwe Hotel Claim). With respect to Community's interests, Fratzke testified that "the department recognizes that the Community has interests and services that it needs to provide to its members and to maintain self governance such as . . . police, fire, taking care of the elderly, children, things like that," and he acknowledged that there are tribal interests in sovereignty and "deriv[ing] revenue." Nichols Decl. 13 (Fratzke Tr.) at 83:3-23; 127:4-6. Fratzke also testified that the Department considers "the Federal interests" which include "the existence of the Tribes and the ability to self-govern, et cetera." *Id*. at 84:1-3. Fratzke conceded that other interests might also be relevant and they

"would need to be raised by the Tribe or whomever was submitting the request . . . those would weigh into that and it's up to the Tribe or the purchaser to submit that information in." *Id*. at 139:18-140:11. Fratzke admitted that he made no effort to learn anything more about tribal or federal interests, and does not know what services the Community provides on or off the Reservation, how it funds the services, or how the economic burden of the Sales Tax impacts the services and funding. *Id*. at 171:23-178:23. Fratzke also testified that the interests deemed relevant by the Department were the same for refund claims submitted by Members as for claims submitted by the Community. *Id*. at 127:9-128-7; 138:8-139:12.

The Department considered only generalized state interests in its "balancing" analysis. As stated in the denial letters, the State claimed an interest because the "taxes are used to fund state and local services for [the Community] and other businesses as well as Michigan's residents (including tribal members)." Nichols Decl. Ex. 14 (May 2014 Claim). Fratzke testified that the services at issue were "firetrucks [that were] available, that there were available police protections, that there was a court system set in place, there were roads put in place." Nichols Decl. 13 (Fratzke Tr.) at 125:4-14.

Fratzke testified that the concept of "essential government functions" plays a critical role in his application of *Bracker* balancing and characterized it as encompassing "all three interests, the Federal interests, the Tribe's interests and the State interests." *Id*. at 159:16-161:5. Indeed, the Department recognizes the Community's Sales Tax immunity *only* for purchases that serve "essential government functions"—and correspondingly, the Department does not recognize Member immunity for *any* purchase. PageID.1696 (Defs. Resp. Interrog. No. 1). Fratzke could not explain the source of the "essential government functions" concept; he testified that it was not drawn from *Bracker* or "any specific case," but stated that "the Department feels that it fits

within that rubric" and "identifies the interests of the State and alters the interests of the State." Nichols Decl. Ex. 11 (Fratzke Tr.) at 169:15-170:4. Fratzke admitted, however, that *Bracker* itself involved a tribe's revenue-raising enterprise—which would not be an "essential government function" according to Defendants: "It was the Tribe's resources . . . it was their land and it was their timber and they were selling that for revenue." *Id.* at 93:3-11.

The Department has denied *all* the claims treated as Sales Tax claims except those involving purchases of property by the Community for use in what the Department views to be an "essential government function." PageID.1696 (Defs. Resp. Interrog. No. 1). Under this rationale, the Department denied *all* Member Sales Tax claims. *Id.*; see also Ex. 1 (2018 Summary Chart). The Department denied *all* Community claims with any perceived connection to revenue-raising activity. All of the Department's denial letters repeated the same basic rationale with only minor variations. Nichols Decl. Ex. 14 (May 2014 Claim) at SOM-FED00005171-72; *see also*, *e.g.*, Ex. 15 (Sept. 2014 Claim) at SOM-FED00010868.

The Department did not exercise any oversight of Fratzke's decisions, or take any other measures to ensure that he was applying federal and state law or Treasury policy correctly. Nichols Decl. 18 (Matelski Tr.) at 58:9-59:21; Ex. 13 (Defs.' Disc. Resp.) at Irog. 33. The Department simply assumed that the Community or members would take on the burden of initiating an appeals process, which would presumably serve to identify and correct any errors of fact or law in the Department's decisions. *Id*. Experience shows that this is inadequate. Defendant Fratzke admitted in a declaration that "Treasury inadvertently overlooked [its own] bulletins when processing [at least 64 of the] claims." PageID.2155 (Fratzke Decl. ¶ 64).

IV. Tobacco Tax and Seizures.

A. The Tobacco Products Tax Act.

During the relevant time period, the Tobacco Products Tax Act ("TPTA"), MCL 205.421-436, imposed a tax on cigarettes of $2 per pack of 20 cigarettes, MCL 205.427(1)(b)-(e). Pursuant to the TPTA, for tobacco transactions subject to the TPTA, the tax was initially paid at the wholesale level, but the statute required the reseller to pass the tax on to the consumer of the tobacco products. MCL 205.427a. Under the TPTA wholesalers or unclassified acquirers of tobacco subject to the act are required to stamp each pack of cigarettes to show that the tax had been paid before the packs were delivered to a retailer for sale. *Id*.

B. Defendants and their Agents Unlawfully Conducted State Law Enforcement Operations against the Community and its Members in the Community's Indian Country.

In the months leading up to December 2015, the Community sold cigarettes at its casinos and convenience stores for which no state Tobacco Tax was paid ("untaxed tobacco"). PageID.3510, 3513-14. The Community acquired the untaxed tobacco from entities outside of Michigan that are wholly-owned by other Indian tribes or tribal members, namely Ho Chunk, Inc. and Native Wholesale Supply. *Ho Chunk, Inc. v. Sessions*, No. 17-5140 at 2 (D.C. Cir., March 15, 2018) ("Ho-Chunk, Inc. . . .is the [Winnebago] Tribe's wholly-owned economic development arm."); Nichols Decl. Ex. 17 (NWS Cert.) at iv.

No later than March 2014, the MSP began conducting surveillance, and possibly other law enforcement operations, on the Community's Reservation against the Community and its members in connection with the Community's acquisition, transportation, and sale of untaxed tobacco. PageID.1437-38; 1459-63; Nichols Decl. Ex. 18 (MSP Rpt.). Defendants carried out surveillance by entering the Reservation without permission or knowledge of the Community, under false pretenses, out of uniform and in an unmarked vehicle, and perhaps through other methods. Nichols Decl. Ex. 19 (Croley Tr.) at 24:2-25:10, 69:23-70:25. Defendant Croley testified at his deposition that from January 1st, 2014 through December 11th, 2015, he

personally conducted surveillance "around 10 to 15 times approximately" within the Reservation, specifically targeting the Community and its members. *Id*. at 82:7-15. The Michigan State Police even cultivated confidential informants to obtain information about the Community's commerce in untaxed tobacco. *Id*. at 122:7-123:21. As shown below, these law enforcement operations against the Community and its members lead directly to seizures of the Community's property, prosecution of its members, and attempts to assess the Tobacco Tax.

C. The Tobacco Acquisitions and Seizures.

1. The December 2015 Seizure.

On or around December 4, 2015, the Community contracted to purchase 3,360 cartons of Seneca brand cigarettes, for $65,620.80, from Ho Chunk, Inc. Distribution ("HCI"), a tribal entity in Nebraska. *Ho Chunk*, No. 17-5140 at 2 (D.C. Cir.). The Community intended to sell the tobacco at its retail locations in its Indian country. PageID.3514. The Community sent a 2015 Ford F-250 pickup truck and 2014 CargoMate utility trailer to transport the cigarettes from HCI's facilities to the Community's Reservation. PageID.3510-11. The truck and trailer belonged to the Community. *Id*.

On December 11, 2015, Defendant Croley and MSP Trooper Ryan were conducting illegal surveillance on the Community's Reservation and spotted a truck and trailer they believed—based on unlawful surveillance—were owned by the Community and used to transport tobacco products. PageID.1437-38. Defendant Croley and Trooper Ryan surveilled the truck and trailer before instructing other MSP Troopers to stop the truck and trailer as soon as they could after the truck left the Community's Indian country. PageID.1439-40. These other Troopers did so, and detained the driver and passenger—Community members and employees John Davis and Gerald Magnant. PageID.1430, 1460-61. At the same time, the Troopers were in contact with the Michigan Attorney General's Office, who directed the Troopers, without a

warrant or consent, to search and seize the boxes in the trailer. PageID.1443. The MSP troopers searched the trailer and found the Seneca brand cigarettes, and, acting on behalf of the Department, seized and inventoried the cigarettes and provided Davis with a "Notice of Seizure and Inventory Statement of Property Seized" ("Notice of Seizure"). PageID.3511.

2. The February 2016 Seizures.

On or about January 28, 2016, the Community purchased 184 cases (11,040 cartons) of Seneca brand cigarettes from Native Wholesale Supply ("NWS"), an entity owned by a Seneca Nation member in New York, for $197,715. PageID.3512-13. The Community intended to sell the tobacco at its retail locations in its Indian country. PageID.3514. NWS arranged for the cigarettes to be shipped, in two shipments of 92 cases each, to the Community's Reservation by XPO Logistics Freight, Inc. ("XPO"). PageID.3512-13. On February 9, 2016, apparently acting on a tip from a confidential informant, an MSP trooper stopped one of the XPO trucks carrying the Community's cigarettes on M-95 near County Road 601 in Marquette County, Michigan. PageID.3512. Another MSP trooper stopped the second XPO truck on U.S. Highway 2 in Iron County, Michigan. PageID.3511. The MSP, acting on behalf of the Department, searched each of the XPO trailers, found 92 cases of the Community's cigarettes in each, and seized them based on the determination that the cigarettes were not stamped. PageID.3512-13. The State attributed a value of $353,280 to the seized cigarettes. *Id*. The Department sent the Community a "Notice of Seizure and Inventory Statement of Property Seized" ("Notice of Seizure") for each seized shipment of cigarettes. *Id*.

3. The State Commenced Criminal Actions Against Community Members and Treasury Issued Notices of Intent to Assess Tax on the Tobacco Products Seized from the Community.

On May 12, 2017, Treasury issued notices of intent to assess tax on the seized tobacco in the amount of $1.728 million. Nichols Decl. 22 (Notices). Further proceedings on the notices of intent to assess have been stayed while this action is pending. *Id*. Ex. 21 (Stay Agmt.).

Defendants Grano, as the prosecutor, and Sproull, as the complaining witness, later commenced criminal prosecutions of the two Community members who were in the truck that was the subject of the December 2015 seizure. (*People v. Davis*, No. 16-05237, and *Magnant*, No. 16-05238, "the State Criminal Prosecutions"). Those actions are pending.

V. Defendants' Current Allegations Regarding Services Provided to the Community and Members and Other Interests in Imposing the Taxes.

As explained above, the Department has enforced the Sales Tax based only on vague notions of the State interests and the bald conclusion that those interests outweigh Community and federal interests. With respect to the Tobacco Tax, Defendants operated on the incorrect assumption that the court "applied *Bracker*" in *Keweenaw Bay Indian Cmty. v. Rising*, 477 F.3d 881, 892 (6th Cir. 2007), and "held that Michigan's interests in imposing the tax clearly outweighed the Community's interests." PageID.1033. It was only for purposes of this litigation that Defendants attempted to actually articulate and define any purported State interests with respect to the Sales or Tobacco Taxes.

A. Defendants Rely on the Report of Treasury Employee Scott Darragh to Establish State Interests.

Apparently realizing the inadequacy of the Department's "balancing" methods and assumptions as a result of this litigation, Defendants obtained the report and testimony of Scott Darragh, Ph.D., an Economic Specialist with the Michigan Treasury's Office of Revenue and Tax Analysis. Darragh claimed the State has a strong interest in imposing the Sales and Tobacco Taxes because those taxes "provide significant revenue for the State of Michigan" and for local governments, which provide services that "enhance the well-being of state residents." Nichols

Decl. 24 (Darragh Tr.) at 53:24-54:10. Darragh testified that all governments—including tribal governments like the Community—have a "vital interest" in generating revenue to support government services. *Id*. at 93:21-94:8. Darragh articulated the State interest broadly and claimed the interest in collecting the Sales Tax on any particular transaction is "strong" because the State relies heavily on such collections generally—not just on the Reservation—for government funding. *Id*. at 56:23-24; 57:4-9. Darragh did not claim to define "State interests" as the term is defined in the *Bracker* analysis. *Id*. at 63:8-13. He discussed the State interests in terms of having a system that raises revenue effectively and efficiently. *Id.* at 96:22-98:21. Darragh does not believe the Community's Sales and Use tax claims put that system at risk, nor are concerns about marketing an exemption—*i.e.*, ensuring a "level playing field" for non-Indian retailers—relevant to the Sales Tax claims. *Id*. at 113:12-20. Darragh agreed the State has no legitimate interest in collecting tax on a transaction where a federal immunity otherwise applies. *Id*. at 62:3-5.

Darragh understood that the Community's claims apply to transactions involving the Community or its members on the Reservation. *Id*. at 70:25-72:5; 82:13-83:17. He also understood that the Reservation does not cover all of Baraga and Marquette Counties and not every resident of the counties is a Community member. *Id*. at 70:25-72:5. In his estimation of the tax revenue at risk, Darragh made no effort to account for the fact that there are only 3,622 Community members, of which only 1,040 live on the Reservation (Swartz Decl. ¶ 3)—he was apparently instructed by Defendants' counsel not to do so. Nichols Decl. 24 (Darragh Tr.) at 88:18-22. Instead, Darragh estimated the total Sales and Tobacco Tax collections from the 74,938 residents of Baraga and Marquette and claimed those amounts—$71.3 million in Sales

Tax and $6.6 million in Tobacco Tax—are at risk in this litigation. *Id*. Ex. 22 (Darragh Tr.) at 70:25-72:5; Ex. 23 (Darragh Rpt.) at SOM-FED00014047-48).

B. Services Allegedly Provided to Community and Members on the Reservation.

Darragh identified several State services that are funded at least in part by sales or Tobacco Tax and are provided in Baraga and Marquette Counties.

- Local government revenue sharing: Cities, villages, and townships receive revenue from the state, some of which is generated by Sales Tax collections. Nichols Decl. Ex. 23 (Darragh Rpt.) at SOM-FED00014060. The revenue is distributed based on the local unit's share of state population. *Id*. Local units may spend the funds they receive for any purpose. *Id*. Defendants do not identify any specific services, to the Community and members or otherwise, that are funded by revenue sharing payments. *Id*.
- Education: Michigan's Kindergarten - l2th grade ("K-12") public education system is funded primarily by the School Aid Fund, which draws revenue from several different state tax collections, including Sales Tax, income tax, property tax, use tax, real estate transfer tax, and Tobacco Tax. *Id*. at SOM-FED00014065). The State Lottery is also a significant source of funding for the K-12 system. *Id*. Michigan also waives the tuition costs for eligible Native Americans at public community colleges or universities in the State. *Id*. Defendants do not identify the source of funding for this program. *Id*. Darragh assumed that because there are public schools near the Reservation, that some Community members living on the Reservation attend the schools. Darragh did not attempt to determine how many actually are attending, or have attended, the schools. *Id*., Ex. 22 (Darragh Tr.) at 144:23-25; 145:5-12. Darragh also did not make any effort to determine how much funding the public schools receive from the Community and federal government—but

admitted he knew that both the Community and federal government provide funding. *Id*. at 146:13-22; 147:5-22.

- Corrections: The Department of Corrections operates facilities in Baraga and Marquette Counties that employ a total of 31 individuals reporting an ethnicity code of "American Indian." Nichols Decl. Ex. 23 (Darragh Rpt.) at SOM-FED00014066. Defendants speculate that one or more of these 31 individuals may be members of the Community.
- Transportation: The State maintains roads throughout Michigan. Road maintenance and improvement is funded primarily by motor vehicle and gasoline taxes—which are not at issue in this litigation. *Id*. at SOM-FED00014059. Darragh did not consider the Community's significant contributions to road projects. *Id*. at SOM-FED00014066-67.
- Economic Development (MEDC): The Michigan Economic Development Corporation (MEDC) engages in economic development efforts throughout the state. MEDC partners with the Community on several projects that benefit the Upper Peninsula. MEDC is funded in part by the Community's 8% payments, and receives significant funding from other Michigan tribes. Nichols Decl. 25 (Darragh Rpt.) at SOM-FED00014067, 69.
- Health and Human Services: Darragh claimed that the State administers, and contributes funding to, "the largest programs providing public assistance" in Michigan, specifically Food Assistance, Medicaid, and Low-Income Home Energy Assistance Programs (LIHEAP). *Id*. at SOM-FED00014067. Darragh claimed that the State funded in part hundreds of thousands of dollars in Medicaid payments to the Community's Health Center and New Day Center. *Id*. at SOM-FED00014068. In fact, the federal government pays 100% of the Medicaid payments for Indians receiving treatment at tribal health facilities. Nichols Decl. Ex. 24 (Medicaid MOA); 32 (THC MOA). Darragh admitted the error in his

deposition, and also admitted that the State contributes virtually nothing to LIHEAP. Nichols Decl. 25 (Darragh Rpt.) at 161:18-163:15; 165:9-166:14; 167:1-8; 167:13-168:6.

- State Police: The Michigan State Police assist (and receive assistance from) the Tribal Police. *Id.* Ex. 23 (Darragh Rpt.) at SOM-FED00014069. The Tribal Police may also make use of the state radio system and dispatch center. According to Darragh's figures, MSP has provided some form of assistance to the Tribal Police about 3 times a month. Tribal Police assist MSP with K-9 unit training, among other things. Swartz Decl. ¶ 11.
- Department of Natural Resources: The DNR has a number of programs to preserve fishing grounds, including some in which it partners with the Community. Nichols Decl. Ex. 22 (Darragh Tr.) at 169:15-170:4; Ex. 23 (Darragh Rpt.) at SOM-FED00014068-69.

VI. The 1842 Treaty.

The Chippewa Indians of the Mississippi and Lake Superior, including the predecessor bands of the Community, signed a treaty on October 4, 1842 (the "1842 Treaty") that ceded to the United States 10,538,000 acres of land, identified in Article I of the 1842 Treaty and consisting of the western half of Michigan's Upper Peninsula and a large portion of Northern Wisconsin, referred to above as the Ceded Area. In consideration of this enormous cession, the United States promised to make a series of payments over a twenty-five year period totaling $875,000. Because the signatory Indian bands expected to remain within the Ceded Area for an indefinite time period, Article II of the 1842 Treaty provided as follows:

> *The Indians stipulate* for the right of hunting on the ceded territory, with the other usual privileges of occupancy, until required to remove by the President of the United States, and *that the laws of the United States shall be continued in force, in respect to their trade and intercourse with the whites, until otherwise ordered by Congress.*

1842 Treaty, art. II (emphasis added).

Article II has never been repealed or abrogated. *Lac Courte Oreilles Band of Lake Superior Chippewa Indians v. Voight*, 700 F.2d 341 (7th Cir. 1983), *cert. denied*, 464 U.S. 805 (1983). The Community's lands comprising the Reservation are located entirely within the Ceded Area, and Michigan's seizures of tobacco products in December 2015 and February 2016 took place in the Ceded Area. PageID.2022 (Reservation is in western half of Upper Peninsula); 3510-12 (seizure locations were in western half of Upper Peninsula).

STANDARD OF DECISION

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, 758 (6th Cir. 2017) (quoting Fed. R. Civ. P. 56(a)).

ARGUMENT

I. Federal Law Preempts Defendants' Imposition of the Sales and Tobacco Taxes with Respect to Transactions in the Community's Reservation (*Counts II and IX*).

A. State Taxes that Adversely Affect Indian Tribes and Members are Preempted by Federal Law Under the *Bracker* Balancing Analysis.

Under the *Bracker* balancing test, in situations in which the legal incidence of a state or municipal tax falls on a non-Indian with respect to property or activities within Indian country but where Indians or Indian tribes are adversely affected by the tax, the tax is preempted if the federal and tribal interests against imposition of the tax outweigh the state's interest in imposing its tax. *Bracker*, 488 U.S. at 143-44; *see also Wagnon v. Prairie Band Potawatomi Nation*, 546 U.S. 95, 101-02 (2005) (confirming that *Bracker* balancing test applies to determine validity of a state tax on a non-Indian if transaction giving rise to tax liability occurs in Indian country).

In applying the balancing analysis, courts examine "the language of the relevant federal treaties and statutes in terms of both the broad policies that underlie them and the notions of sovereignty that have developed from historical traditions of tribal independence" in an inquiry

that "is not dependent on mechanical or absolute conceptions of state or tribal sovereignty, but has called for *a particularized inquiry into the nature of the state, federal, and tribal interests at stake*, an inquiry designed to determine whether, in the specific context, the exercise of state authority would violate federal law." *Bracker*, 488 U.S. at 144-45 (emphasis added). In this framework, "[s]tate jurisdiction is pre-empted by the operation of federal law if it interferes or is incompatible with federal and tribal interests reflected in federal law, unless the State interests at stake are sufficient to justify the assertion of state authority." *New Mexico v. Mescalero Apache Tribe*, 462 U.S. 324, 334 (1983). Unlike the standard federal preemption test, federal preemption of state jurisdiction over Indians "is not limited to those situations where Congress has explicitly announced an intention to pre-empt state activity." *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). "[T]he traditional notions of tribal sovereignty, and the recognition and encouragement of this sovereignty in congressional Acts promoting tribal independence and economic development, inform the pre-emption analysis that governs this inquiry." *Id.* (citing *Bracker*, 448 U.S. at 143 & n.10). Treaties and federal statutes must be interpreted "generously in order to comport with these traditional notions of sovereignty and with the federal policy of encouraging tribal independence." *Bracker*, 448 U.S. at 144-45.

The federal government has interests in tribal economic development and tribal self-government, stated explicitly in numerous Acts of Congress and Executive Branch policies and programs. *See,* Indian Reorganization Act, 25 U.S.C. §§ 461 *et seq*., the Indian Self-Determination and Educational Assistance Act ("ISDEAA"), 25 U.S.C. § 5301 *et seq.*, Indian Financing Act of 1974, 25 U.S.C. § 1451 *et seq.*; *see also* Presidential Memorandum of November 9, 2009: Tribal Consultation, 74 Fed. Reg. 57881 (Nov. 9, 2009); Presidential

Executive Order 13175, 65 Fed. Reg. 67249, Consultation and Coordination with Indian Tribal Governments, § 2(a), (Nov. 6, 2000). Federal interests are strongest when a comprehensive and pervasive federal regulatory scheme governs the activity burdened by the tax. *See Ramah*, 458 U.S. at 841-44; *Bracker*, 448 U.S. at 151.

Tribal governments share the federal government's interests in tribal economic development and tribal self-government, and these tribal interests especially strong when the revenues burdened by the tax are derived from value "generated on the reservations by activities in which [Indians] have a significant interest." *Washington v. Confederated Tribes of the Colville Indian Reservation*, 447 U.S. 134, 155 (1980); *accord Indian Country, U.S.A., Inc. v. Oklahoma*, 829 F.2d 967, 986 (10th Cir. 1987). The tribal interests are virtually decisive if the tribe or a tribal member bears the direct economic burden of the tax. *See Ramah*, 458 U.S. at 844; *Bracker*, 448 U.S. at 151.

Though states have an interest in raising revenue, that interest is at its weakest when the tax is not imposed to compensate the state for services provided within the reservation to the taxpayer or to the activity affected by the tax. In *Bracker*, the Supreme Court examined the state's regulatory interest and services provided to a non-Indian logging company which bore the legal incidence of the motor carrier license and use fuel taxes that Arizona imposed on the company's on-reservation activities. The *Bracker* court concluded that Arizona could not identify "any regulatory function or service performed by the State that would justify the assessment of taxes for activities on Bureau and tribal roads within the reservation." 448 U.S. at 148-49. In *Ramah*, the Court attached little importance to the *off*-reservation services provided by the state to the non-Indian contractor (Lembke), noting that"[p]resumably, the state tax revenues derived from Lembke's off-reservation business activities are adequate to reimburse the

State for the services it provides to Lembke." 458 U.S. at 844 n.9; *New Mexico*, 462 U.S. at 336 (holding that exercise of state authority must be justified by state functions or services in connection with on-reservation activity).

Thus, state taxes are unlawful under any of the following circumstances: the tax intrudes on federal government regulation intended to benefit a tribe, the tax burdens reservation value in which a tribe has a significant interest, the economic burden of the tax falls directly on a tribe or the tax is imposed without relation to a state service provided on the reservation to the taxpayer or to the activity burdened by the tax. *Ramah,* 458 U.S. at 841-44; *Bracker*, 448 U.S. at 151; *see, e.g.*, *and compare Cotton Petroleum Corp. v. New Mexico*, 490 U.S. 163, 185-87 (1989) (tax on non-Indian company lawful where federal regulation of the industry was not exclusive, tax did not impose any direct economic burden on the tribe, and State directly provided the company with services for its operations). Moreover, courts routinely decide balancing claims on summary judgment. *E.g.*, *Bracker*, 448 U.S. at 140-141 (appeal of summary judgment); *Flandreau Santee Sioux Tribe v. Sattgast*, 2018 U.S. Dist. LEXIS 117706, *4, __ F. Supp. 3d __, (D. S.D. 2018) (granting summary judgment on tribe's *Bracker* challenge to general excise tax on contractor).

B. The Community and Federal Interests Outweigh Any State Interest in Imposing the Sales Tax on the Community and Members with Respect to Transactions on the Reservation.

As explained in the Community's First SJ Memorandum, the holding in *Warren Trading Post Co. v. Arizona Tax Commission*, 380 U.S. 685 (1965)—as affirmed in *Central Machinery Co. v. Arizona Tax Commission*, 448 U.S. 160 (1980)—regarding the preemptive effect of the Indian Traders Statutes as to sales on the Reservation is settled law. PageID.1616-28 (citing *Bracker*, 448 U.S. at 144, 151). State taxation of transactions between Indian traders and Indian tribes and tribal members is categorically preempted. *Id*. (citing *Central Machinery*, 448 U.S. at

165-66). Nevertheless, Defendants have ignored the categorical rule and insisted that the state (not the court) must perform *Bracker* balancing and must do so for each separate purchase by the Community and its members on the Reservation. As explained below, Defendants do not apply *Bracker* balancing, but decide the claims based on legally incorrect rules of their own invention. Even if this Court were to revisit the *Warren Trading* and *Central Machinery* holdings and balance interests with respect to the Sales Tax, the Court should confirm that the Community's and federal interests clearly outweigh any relevant state interests supporting imposition of the Sales Tax, and, based on the interests at stake, the outcome is the same for all such transactions in the Community's Indian country.

1. The Sales Tax is Imposed on Reservation Activity and the Community and Members Bear the Economic Burden of the Tax.

All of the transactions at issue involve purchases by the Community or members that either took place entirely on the Reservation, or in which the order was placed from the Reservation, payment was remitted from the Reservation, and the goods or services were delivered to the Reservation. Nichols Decl. Ex. 1 (2018 Summary chart); Swartz Decl. ¶ 22; S. LaFernier Decl. ¶ 3-4; M. LaFernier Decl. ¶ 3-4; E. Mayo Decl. ¶ 3-4; S. Mayo Decl. ¶ 3-4. Under established contract law and the Sales Tax Sourcing Rule—a generally applicable statute that determines the location of a transaction for Sales Tax purposes—the transactions took place on the Reservation. *See* Mich. Comp. Laws §§ 205.69, 205.110. In each of the Exemplar Claims, the Community or Member sought a refund on the basis of a receipt or invoice that itemizes the price of the good or service being acquired and the amount of Sales Tax, and sought a refund only of the itemized Sales Tax amount. Nichols Decl. Ex. 1 (2018 Summary chart).

The Court's inquiry should end at this point: tribal interests are virtually decisive if the tribe (or a tribal member) bears the direct economic burden of the tax. *See Ramah*, 458 U.S. at

844; *Bracker*, 448 U.S. at 151.

2. The Community Bears the Economic Burden of the Sales Tax and that Injures the Community's Interests in Sovereignty, Self-Governance, and Providing Governmental Services.

The Supreme Court has already recognized that Indian tribes like the Community have strong interests in self-determination, self-governance, and economic development. *Bracker*, 448 U.S. at 149. The Court also has noted that tribes have an especially strong interest in value "generated on the reservation[] by activities in which [it has] a significant interest." *Colville*, 447 U.S. at 155; *Indian Country*, 829 F.2d at 986. Here, the Community's revenue-raising enterprises—the Gaming Enterprises, service stations, radio stations, and others—play a critical role in supporting the Community's self-determination and economic development goals. The Community has invested millions of dollars in its enterprises, and they are government services in their own right, providing employment opportunities for members and generating economic activity on the Reservation. Swartz Decl. ¶ 16. The enterprises also fund the Community's essential government programs and services provided to the Reservation community, including tribal members and other residents, visitors, employees, and vendors. *Id.*

The Community operates no fewer than 20 departments that provide government services to its members, including healthcare, governance, law enforcement, public utilities, employment rights, social services, education, and others. *See* Undisputed Facts, II.A-B, *supra*. Some of these services benefit from federal funding, but the Community could not provide the full slate of programs and services with federal funding alone. Revenues from the Community's enterprises account for as much as 66% of its annual government budget and the Gaming Enterprises alone employ more than one hundred Community members. Nichols Decl. Ex.'s 3-7 (Bdgt. FY12 – Bdgt. FY16); 31 (Empl. Data). The Community's enterprises, and the revenues they generate, are therefore vitally important to fostering tribal self-determination and economic development.

See California v. Cabazon Band of Mission Indians, 480 U.S. 202, 218-20 (1987) (tribal gaming is a means to fund "tribal governments and the provision of tribal services" and without it, "[s]elf-determination and economic development are not within reach.").

There is no dispute that the Community and its members bear the economic burden of Sales Tax in their purchases on the Reservation. When the Community is required to pay the tax, it decreases the funds available to provide government programs, services, and economic development efforts. Swartz Decl. ¶ 25. Likewise, Community members have fewer resources to invest in their livelihood on the Reservation and the Reservation economy. *Id*. Even Defendant Fratzke admitted that there is an economic burden when the Community pays unrefunded Sales Tax on a purchase: the Community loses the power to decide how that money will be spent—the Community cannot use it to fund economic development, pay salaries, or provide services—instead, the State decides how to spend the money collected from the Community. Nichols Decl. Ex. 11 (Fratzke Tr.) at 180:7-18. Defendants' proffered expert, tax analyst Scott Darragh agreed. *Id*., Ex. 22 (Darragh Tr.) at 182:1-19.[4]

The injury to the Community's interests is not solely economic in nature. Deciding when and how to exercise the power of taxation is a fundamental element of governance. Nichols Decl. Ex. 2 (Henson Rpt.) ¶ 45; *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130, 137 (1982) ("The power to tax is an essential attribute of Indian sovereignty because it is a necessary instrument of self-government. . . [it] derives from the tribe's general authority, as sovereign, to control economic activity within its jurisdiction."). The power to tax applied in the right way can

[4] Defendants proffered an economic development "expert" who claimed that bearing the economic burden of the Sales and Use Taxes does not impede the Community's economic development, but the expert also admitted that she did not understand how state tax burdens affect businesses. Nichols Dec. 33 (Benton Tr.) at 129:9-132:24. She could not (or would not) even explain what "tax burden" means. *Id*. at 132:20-24.

advance economic development goals and support governmental services. Nichols Decl. 2 (Henson Rpt.) ¶ 45. But if the power of taxation is applied without due consideration, then it can undermine those same goals. *Id*. ¶ 48. Thus, when the Community cannot decide what activity on the Reservation will be taxed, how much it will be taxed, or where the tax revenue will go, that undermines the Community's ability to self-govern. *Id*. ¶¶ 45-50. This injury is compounded by the fact that, as shown in Part I.B.4, below, the State's Sales Tax collections fund activities with little or no connection to Reservation activity.

The Community's interests apply with equal force to refund and exemption claims submitted by Community members. *Bracker*, 448 U.S. at 143-44 (tribal interests in self-sufficiency and economic development include activity by tribe and members); *see, e.g. Oneida Nation of N.Y. v. Cuomo*, 645 F.3d 154, 171 (2nd. Cir. 2011) (no distinction between the interests of the tribe and the interests of its individual tribal members in conducting *Bracker* balancing analyses).[5] The Community also has a strong interest in ensuring that its members have the resources needed to live on the Reservation as active members of the Community. Swartz Decl. ¶ 27. The vitality of the Community as a self-governing tribe is dependent on creating and protecting a high-quality of life on the Reservation. *Id*. Fewer than one third of Community members live on the Reservation now, and that is something that the Community wants to change to ensure that it continues as a self-governing tribe long into the future. *Id*.

3. The Sales Tax Interferes with the Federal Interest Demonstrated in at Least Three Comprehensive Federal Regulatory Schemes.

Federal policy encourages American Indian economic development, self-governance and

[5] The tribe's interest represents the "collection of individual interests" of its members. *United States v. Michigan*, 471 F. Supp. 192, 226 (W.D. Mich. 1979); *see also United States ex rel. Steele v. Turn Key Gaming, Inc.*, 135 F.3d 1249, 1252 (8th Cir. 1998) (noting that the interests of the Indian tribe and its member were identical).

self-determination. Preserving the Community's control of governmental, socioeconomic, and business development on its Reservation—including with respect to taxation of transactions involving and affecting the Community and its members—aligns with and advances these Federal policies. Nichols Decl. 2 (Henson Report) ¶¶ 42-45; *see also e.g.*, Presidential Executive Order 13175, 65 Fed. Reg. 67249, Consultation and Coordination with Indian Tribal Governments, § 2(a), (Nov. 6, 2000). Additionally, at least three comprehensive federal schemes, the Indian Trader Statutes, the Indian Gaming Regulatory Act ("IGRA"), and ISDEAA establish the federal government's strong interest against imposition of the Sales Tax in the circumstances here.

(a) *The Federal Government Comprehensively Regulates Trade with Indians through the Indian Trader Statutes.*

The federal government comprehensively regulates all trade with Indian tribes. As shown in the Community's First SJ Memorandum (PagedID.1616-28), the Indian Trader Statutes give the federal government exclusive authority to regulate non-Indians trading with Indians on a reservation. 25 U.S.C. §§ 261-264; 25 C.F.R. pt. 140. The Supreme Court has repeatedly held that the Indian Trader Statutes categorically bar a state from imposing a transaction or excise tax—like the Sales 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. *Central Machinery*, 448 U.S. at 160; *Warren Trading*, 380 U.S. at 690. As explained in the Community's First SJ Memorandum, the Court should find that the Indian Trader Statutes categorically bar Defendants' imposition of the Sales Tax, but if it does not, the Indian Trader Statutes demonstrate a strong federal interest against imposing the tax.

(b) *The Federal Government Comprehensively Regulates Gaming-Related Transactions with Indians through IGRA.*

IGRA was enacted to further "a principal goal of Federal Indian policy [which] is to promote tribal economic development, tribal self-sufficiency, and strong tribal government." 25 U.S.C. § 2701(4). IGRA establishes "a comprehensive regulatory structure for Indian gaming." *Gaming Corp. of Am. v. Dorsey & Whitney*, 88 F.3d 536, 544 (8th Cir. 1996). Federal regulation of tribal gaming leaves the states with "no regulatory role over [tribal] gaming except as expressly authorized by IGRA" and even then, only so far as permitted by "a tribal-state compact." *Id.* at 546. It establishes the primacy of tribal and federal "regulation of gaming activities on Indian lands" and does not allow state regulation "unless a tribe affirmatively elects to have State laws and State jurisdiction extend to tribal lands." S. Rep. No. 100-446, at 5-6 (1988), *reprinted in* 1988 U.S.C.C.A.N. 3071, 3075. IGRA "provide[s] a statutory basis for the operation of gaming by Indian tribes as a means of promoting tribal economic development, self-sufficiency, and strong tribal governments," 25 U.S.C. § 2702(1), and affirms the Indian tribes' "exclusive right to regulate gaming activity on Indian lands" under IGRA's framework, 25 U.S.C. § 2701(5).

This comprehensive regulatory scheme encompasses taxation of transactions involving tribal gaming enterprises. IGRA specifically addresses the role of state taxation in the context of tribal gaming operations. It provides a means for states to recover the cost of regulatory services provided in connection with tribal gaming; specifically tribal-state compacts may include "assessment[s] by the State . . . in such amounts as are necessary to defray the costs of regulating such activity." 25 U.S.C. § 2710(d)(3)(C)(iii). To this end, the Community has agreed to contribute a total of 10% of its net win to state and local government agencies. Nichols Decl. Ex. 8 (MGCB Rpt.). But IGRA prohibits a State from "impos[ing] any tax, fee, charge, or other assessment upon an Indian tribe or upon any other person or entity authorized by an Indian tribe

to engage in a class III activity," 25 U.S.C. § 2710(d)(4). This ensures that intended benefits of tribal gaming enterprises flow to the tribes, and not state or local taxation. *Breakthrough Mgmt. Group, Inc. v. Chukchansi Gold Casino & Resort*, 629 F.3d 1173, 1192 (10th Cir. 2010) (IGRA "ensure[s] that the Indian tribe is the primary beneficiary of the gaming operation."); *see Sattgast*, 2018 U.S. Dist. LEXIS 117706, at *4 (state tax on contractor for services to tribal gaming enterprise preempted based on federal and tribal interests set forth in IGRA).

Defendants' refusal to recognize any Sales Tax immunity for the Community's gaming enterprises clearly violates the express language of IGRA—Defendants denied every single one of the Exemplar Claims submitted by Community for purchases for its Gaming Enterprises. Nichols Decl. Ex. 1.

(c) *The Federal Government Comprehensively Regulates and Encourages the Tribal Self-Government and Economic Development through ISDEAA.*

ISDEAA established a framework for the "transition from the Federal domination of programs for, and services to, Indians to effective and meaningful participation by the Indian people in the planning, conduct, and administration of those programs and services" and "supporting and assisting Indian tribes in the development of strong and stable tribal governments, capable of administering quality programs and developing the economies of their respective communities." 25 U.S.C. § 5302(b). The federal government historically fulfilled its trust responsibility to tribes by providing certain government services directly, and now supports and funds tribal governments in designing and operating the programs for themselves. *Id*. The Community operates healthcare, law enforcement, and court programs under ISDEAA compacts and contracts. Swartz Decl. ¶ 4. The State cannot tax purchases by federal agencies operating those programs, *United States v. California*, 507 U.S. 746, 753 (1993), but the State claims the right to tax nearly all such transactions carried out by the Community.

Though the ISDEAA programs receive significant federal funding, the amounts are sometimes not sufficient to implement the programs and the Community also contributes funding. Nichols Decl. Ex.'s 2-7 (Bdgt. FY12 – Bdgt. FY16). There is a strong federal and Community interest in ensuring that the Community is able to supplement the funding for those programs in that event. Swartz Decl. ¶¶ 22-25; 25 U.S.C. § 5302(b). When the Community's revenue-raising activities are forced to divert funds to the Sales Tax, that interest is undermined.

Federal interests and policies strongly favor the Community's self-governance, self-determination, and economic development and weigh heavily against Defendants imposing the Sales Tax on the transactions at issue here.

4. The State Cannot Identify any Interests Sufficient to Justify Imposition of the Tax.

Defendants' handling of the Community and Members' Sales Tax Refund applications turned on their determination of whether the Community was making the purchase and doing so for an "essential government service"—if so, Community and federal interests prevailed, and if not, State interests prevailed. This is not a legally correct application of *Bracker* balancing and Defendants cannot otherwise identify any legitimate interest for imposing the Sales Tax.

(a) *The "Essential Government Services" Concept has No Place in the Balancing Analysis—Defendants Invented it with No Basis in Federal Law.*

Defendants created out of whole cloth the "essential government services" concept to justify imposing the Sales Tax on transactions involving any revenue-raising activity by the Community as well as every transaction by Community members. Defendants cannot identify any case law or other authority as a source for the concept. Nichols Decl. 13 (Fratzke Tr.) at 169:15-170:4. In fact, Defendants' use of the concept contradicts established Supreme Court precedent. *Bracker*, 448 U.S. at 139, and *Central Machinery*, 448 U.S. at 161, involved

transactions by tribal revenue-raising enterprises, and *Warren Trading* involved a non-tribal retail store that sold to tribal members. 380 U.S. at 686. The Supreme Court confirmed that state taxes on those tribal revenue-raising enterprise transactions and on tribal member transactions were preempted in all three cases. Defendant Fratzke even admitted that he knew *Bracker* involved a tribe's revenue-raising operations, but nonetheless relied on this as a factor in his application of *Bracker* balancing to deny tax immunity to every transaction involving the Community's enterprises. Nichols Decl. 13 (Fratzke Tr.) at 93:3-11.

Not only is their "essential governmental services" concept a self-serving fiction without any basis in federal Indian law, Defendants have denied exemptions even to departments of the Community's government that are not involved in revenue-raising activity. Nichols Decl. Ex. 1 (2018 Summary Chart) (Maintenance Dept. (lines 401, 492), Tribal Center (line 1251), Community Assistance Program (numerous)). Defendants also denied exemptions to the Gaming Enterprises, which as explained above, play a critical role in developing the Community's economy and funding its government. *Id*. (Summary Chart at lines 98-100, and others). The "essential government services" concept is simply a tool that allows Defendants to arbitrarily denigrate important tribal interests (generating revenue for government services, encouraging economic development on the Reservation and ensuring that members have the resources needed to live on the Reservation as active members of the Community), and elevate irrelevant or weak State interests (ensuring a "level playing field for non-Indian businesses and general administration of the tax system").

(b) *The State Cannot Otherwise Identify any Legitimate Interest that Weighs in Favor of Imposing Sales Tax on Reservation Transactions.*

The State must show a "specific, legitimate regulatory interest" to justify the imposition of its tax. *Ramah*, 458 U.S. at 843; *Bracker*, 448 U.S. at 150. This requires a showing of a

nexus between the activity taxed and the services provided by the State. *Mescalero*, 462 U.S. at 336 ("The exercise of State authority which imposes additional burdens on a tribal enterprise must ordinarily be justified by functions or services performed by the State in connection with the on-reservation activity."). A "State seeking to impose a tax on a transaction between a Tribe and nonmembers must point to more than its general interest in raising revenues." *Id.* at 336. Defendants failed to even come close to meeting this standard in their handling of the Sales Tax Refund and Exemption Claims.

In addition to the invented "essential government services" concept, Defendants relied on generalized statements of the need for revenue to justify collecting the tax. Defendants stated the Sales and Use "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." Nichols Decl. Ex. 14 (May 2014 Claim) at SOM-FED00005171-72; *see also*, *e.g.*, Ex. 15 (Sept. 2014 Claim) at SOM-FED00010868. Some denial letters relied on factors that had nothing to do with activity or services on the Reservation, but on "speculation" regarding the economic impact on non-Indians of recognizing the exemption—they include the assertion that "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. 26 (Oct. 2015 Claim) at SOM-FED00008409. Fratzke admitted that this concern was based on "speculation"—and then denied that it was even a factor in deciding the Refund and Exemption Claims. Nichols Decl. 13 (Fratzke Tr.) at 39:10-40:14; 45:11-15. Defendants' proffered expert, tax analyst Scott Darragh, confirmed that when the Community or a member is the purchaser, concerns about "marketing an exemption" are not relevant to the State's interests. Nichols Decl. 24 (Darragh Tr.) at 113:12-20.

Unlike Fratzke, Darragh attempted to look past generalized state interests. In doing so, he managed to identify a few State services that are provided on the Reservation (and a handful of others that *might* be), but neither he nor Defendants can connect those to any legitimate regulatory interest in imposing the Sales Tax on the transactions at issue.

State Roads. Darragh identified road maintenance and construction as a service that might support a State interest in imposing the Sales Tax on transactions on the Reservation (Fratzke also made vague references to road work in some denial letters). Nichols Decl. 25 (Darragh Rpt.) at SOM-FED00014066. But the State funds road maintenance almost entirely from motor vehicle and gasoline taxes, which are not at issue in this litigation. *Id*. at SOM-FED00014059. Moreover, the Community makes significant—more than $1.5 million since 2015—financial contributions to road projects on or near the Reservation. Nichols Decl. Ex. 10 (Road Contrib.); Ex. 23 (Darragh Rpt.) at SOM-FED00014066.

Additionally, the State would need to maintain the roads at issue, whether or not the Community or members used them at all, because the roads connect Michigan cities and are essential for transit through the state. For example, M-38 does not just go past the Ojibwa Casino in Baraga; it serves the larger purpose of connecting the majority non-Indian populations of Baraga and Ontonagon, MI, as well as several other cities and towns in between, and allows a direct westward route for Michigan residents and visitors to travel across the northern Upper Peninsula. Nichols Decl. 29 (M-38 Road Map). By Defendants own estimation, the roads serve populations where the vast majority of residents are non-Indian—there are 74,938 residents in Baraga and Marquette Counties, but only 3,622 Community members total (living anywhere). Nichols Decl. 25 (Darragh Rpt.) at SOM-FED00014047.

Education. Darragh identified education, especially public K-12 schools, as services that

might support a State interest in imposing the Sales Tax on transactions on the Reservation. *Id.* at SOM-FED00014064-66. Defendants do not allege, however, the required connection between providing education and the carrying-out of transactions on the Reservation. *Mescalero*, 462 U.S. at 336. In any event, Sales Tax collections do support education, but, as Darragh admits, the Community also contributes to local public schools—more than $100,000 per year since at least 2012, and the federal government also provides education funding. Nichols Decl. 24 (Darragh Tr) at 147:5-17; Ex. 10 (School Contrib.). Darragh does not know, and made no effort to determine, how many school-age Community members live on the Reservation or which public schools they might attend. Nichols Decl. 24 (Darragh Tr) at 145:5-12.

Defendants cannot establish that imposing the Sales Tax is justified as compensation for services provided on the Reservation to the Community, members, or retailers who engage in the activities subject to the tax. *Bracker*, 448 U.S. at 148-49 (finding that state cannot impose tax where it could not identify "any regulatory function or service performed by the State that would justify the assessment of taxes for activities" on the reservation); *Ramah*, 458 U.S. at 844 n. 9 (rejecting the argument that off-reservation services provided by the State are relevant to the balancing analysis). Accordingly, Defendants have not, and cannot, establish a State interest in imposing the Sales Tax that outweighs the Community and federal interests against it.

C. The Community and Federal Interests Outweigh Any State Interest in Imposing the Tobacco Tax on the Community's Sales of Tobacco at its On-Reservation Establishments.

Defendants have long relied, mistakenly, on the belief that they can require the Community to purchase only tax-prepaid and stamped tobacco products and then seek a refund for sales to tribal members, and that Defendants or their agents may seize untaxed tobacco products in transit to the Community. PageID.1025. Defendants contend, incorrectly, that the court "applied *Bracker*" in *Keweenaw Bay Indian Cmty. v. Rising*, 477 F.3d 881, 892 (6th Cir.

2007), and "held that Michigan's interests in imposing the [Tobacco] tax clearly outweighed the Community's interests." PageID.1033. As this Court recognized, the Sixth Circuit did not even mention *Bracker* or *Bracker* balancing in its decision; rather, it correctly noted that the Community was not litigating the question whether the TPTA was preempted under *Bracker* balancing. PageID.1181; *Rising,* 477 F.3d at 890 n.3, 886-92. The Community is litigating that question now. Contrary to Defendants' conclusory assertions and misplaced reliance on the *Rising* decision, the Community has strong interests in self-determination, self-sufficiency, and economic development that support its right to sell untaxed tobacco. Defendants cannot identify any State interest adequate to justify their efforts to usurp the value created on the Reservation by the Community's development of its tobacco retail business.

1. The Community's Tobacco Business Creates Significant Value on the Reservation and Contributes to the Community's Self-Determination and Economic Development.

The Community's sale of untaxed tobacco makes a significant contribution to the Community's efforts to achieve self-determination and maximize the potential for economic development. The Community therefore has strong interests, which are shared by the federal government, in being allowed to continue that business without interference from Defendants.

The Community has an especially strong interest in value "generated on the reservation[] by activities in which [it has] a significant interest." *Colville*, 447 U.S. at 156-57; *Indian Country*, 829 F.2d at 986. This is especially true for the Community's sale of untaxed tobacco because all of the revenue goes to the General Welfare Support Program which provides a payment for eligible Tribal Members as reimbursement for certain expenses, generally in the form of a "Christmas Gift" distribution to Community members. Nichols Decl. 30 (Tob. Code) at KBIC_TAX0009819. The Community made significant investments—millions of dollars—to create the Gaming Enterprises and service stations where it sells tobacco products, and the

Community's tobacco sales at those establishments meet a demand that the Community created. Nichols Decl. Ex. 2 (Henson Rpt.) at 7, 14. Tobacco products are complements to gaming, and many casino patrons feel that their gaming experience is enhanced by the use of tobacco. *Id*. at 24-26. Similarly, many service station customers expect to be able to purchase tobacco products at the same time they purchase gasoline. *Id*.

There can be no dispute that imposing the Tobacco Tax burdens the Community and its pursuit of self-determination and economic development. Paying the tax increases the Community's cost of acquiring products, and the Community must therefore absorb the cost of the tax, and thus lose revenue, or pass the tax on to the consumer. *Id*. at 20. If the Community passes the tax onto consumers, that leads to a decrease in the quantity that consumers are able to purchase. *Id*. In either event, the Community loses revenue that would otherwise contribute directly to the welfare of its members, thereby advancing the goals of economic development and self-determination. *Id*. In addition, the Community would likely lose customers at its casinos, hotel, and service stations—customers that value the Community's sale of untaxed tobacco to complement the gaming experience might be more inclined to take their business elsewhere if the Community could no longer offer that amenity. *Id*.

2. Defendants Cannot Identify a Legitimate State Interest in Imposing the Tobacco Tax on the Community's Sales.

In contrast, Defendants cannot identify a legitimate State interest in taxing the Community's sale of tobacco products on the Reservation. Just as they do with the Sales Tax, Defendants focus on a generalized interest in raising revenue and administering the tax system, but this is not a legitimate state interest under the *Bracker* balancing analysis. *Mescalero*, 462 U.S. at 336 ("State seeking to impose a tax on a transaction between a Tribe and nonmembers must point to more than its general interest in raising revenues.") Tobacco Tax collections

primarily go to the General Fund, School Aid, and the Medicaid Trust Fund. Nichols Decl. 25 (Darragh Rpt.) at SOM-FED00014047. Smaller allocations support other statewide health/safety programs, State Police, the Capitol Historic Fund, and Wayne County Indigent Care. *Id*. None are sufficient to establish the specific, legitimate regulatory interest that would be needed to justify the imposition of its tax. *Ramah*, 458 U.S. at 843; *Bracker*, 448 U.S. at 150. Specifically:

- Generating revenue for the General Fund is not a legitimate state interest under *Bracker* balancing. *Mescalero*, 462 U.S. at 336.
- Funding the Medicaid Benefits Trust funds a portion of the State's Medicaid expenditures. Nichols Decl. 24 (Darragh Tr.) at 141:9-20. This has no nexus to services provided to the Community or members on the Reservation, because, as shown in Facts Part V.B, above, the federal government pays 100% of Medicaid payments to the Community clinics for treatment of Medicaid-eligible Indians.
- The same flaws that apply to Defendants' attempt to use education programs as justification for the Sales Tax also apply to any attempt to rely on the same programs to justify the Tobacco Tax. As explained in Part I.B, the State and local governments are adequately compensated—outside of Tobacco Tax collections—by the Community for any educational services provided.

Defendants do not, and cannot, establish an interest in imposing the Tobacco Tax on the transactions at issue that outweighs the strong Community and federal interests in self-determination and economic development.

II. Defendants' Imposition of the Sales and Tobacco Taxes Infringes the Community's Rights of Tribal Self-Government and Sovereignty (Counts III, X, and XIV).

A. Tribal Sovereignty is an Independent Barrier to Defendants' Imposition of the Sales, Use, and Tobacco Taxes.

Tribal sovereignty is an independent barrier to the exercise of a state's authority if it

"unlawfully infringe[s] 'on the right of reservation Indians to make their own laws and be ruled by them.'" *Bracker*, 448 U.S. at 142 (citing *Williams*, 358 U.S. at 220). The power to make decisions about taxation on the reservation is "[c]hief among the powers of sovereignty recognized as pertaining to an Indian tribe" and "this power may be exercised over members of the tribe and over nonmembers." *Colville*, 447 U.S. at 153. The Community has made deliberate choices about the laws and regulations it enacts in order to regulate activities on the Reservation in the manner the Community, through its governing body – the Tribal Council – deems appropriate. Swartz Decl. ¶ 5. Without legal basis, Defendants attempt to enter the Reservation and usurp the Community's authority to make or modify that tax decision by imposing their own Sales, Use[6], and Tobacco Taxes on activities in the Community's jurisdiction – a tax that benefits the State, not the Tribe. There can be no greater infringement on the Community's sovereign authority than another government seeking to enter the Community's jurisdiction and impose a tax on the Community and members' activity—everything from providing government services to members' purchases of clothing and other essentials.

B. Defendants' Law Enforcement Operations on the Reservation Infringe the Community's Sovereignty and Right of Self-Government.

Defendants have admitted to conducting surveillance and investigations against the Community and its members on the Reservation. The December 11, 2015 stop and seizure, along with the State Criminal Prosecutions, were the direct result of surveillance conducted on the Reservation against the Community and members by Defendant Croley and MSP troopers under his command. Nichols Decl. 21 (Croley Tr.) at 40:13-42:14.

It is a well-established principle of federal Indian law that states like Michigan have no

[6] As explained in the Community's First SJ Motion, the legal incidence of the Use Tax falls on the Community and members, and is therefore categorically barred as a matter of federal law—the balancing analysis does not apply. PageID.1629-31.

jurisdiction to conduct law enforcement activity of any kind against the Community and its members on Reservation and trust lands—the State cannot conduct surveillance or other investigative activities, and it cannot make arrests. *U.S. v. Peltier*, 344 F. Supp. 2d 539, 546-47 (E.D. Mich. 2004); *State v. Cummings*, 679 N.W.2d 484, 487-89 (S.D. 2004) (both holding that state police officers cannot conduct an on-Reservation search even with a warrant or in connection with alleged off-Reservation crimes); *see also Saginaw Chippewa Indian Tribe v. Granholm*, No. 05-10296, 2011 U.S. Dist. LEXIS 53765, at *9 (E.D. Mich. May 18, 2011) (indicating that *Cummings* properly articulated the scope of state police authority in Indian country); *Moses v. Dep't of Corr.*, 736 N.W. 2d 269, 279 (Mich. Ct. App. 2007) (accepting that Michigan police do not have jurisdiction to conduct investigations or make arrests in Indian country); *Rodewald v. Kan. Dep't Revenue*, 297 P.3d 281, 289-91 (Kan. 2013) (holding that State lacked jurisdiction to investigate drunk driving offenses on the Reservation because "a state has no civil or criminal jurisdiction over tribal members unless Congress has expressly said so").

Defendants' conduct here is even more offensive to tribal sovereignty than the conduct at issue in *Cummings* and *Peltier*. In *Cummings*, a state officer was engaged in an off-Reservation investigation, aimed at regulating off-Reservation conduct, and followed the suspect onto a Reservation. The court still found the tribe's sovereignty was injured by the State's attempt "to extend its jurisdiction into the boundaries of the Tribe's Reservation without consent" and tribal sovereignty was properly invoked "as a shield to protect the Tribe's sovereignty from incursions by the State." *Cummings*, 679 N.W.2d at 487. The injury was serious, and the court imposed an appropriate consequence – suppressing all evidence obtained from the unlawful on-Reservation investigation. *Id*. Similarly, in *Peltier*, the court found that a warrant to search an on-Reservation home in connection with suspected controlled substance and fire-arms offenses

outside the Reservation was not valid. 344 F. Supp. 2d at 546. But there was nothing in either case to suggest that the state officers' conduct was part of a larger effort to regulate the activities of the Tribe or its members on the Reservation. *Id*. In this case, Defendants started an unlawful on-Reservation investigation to regulate the Community's tobacco commerce on its own Reservation. Defendants' conduct on its own is a recognized injury to the Community's sovereign rights, and the injury is compounded because it interferes with the Community's ability to carry out activities that are within its federal rights and are a critical component of its self-determination and economic development efforts. *See* Part I.C, *supra*.

III. Article II of the 1842 Treaty Preempts, within the Area Ceded by the 1842 Treaty, Defendants' Imposition of Sales Taxes, Use Taxes and Tobacco Taxes on Transactions Involving the Community or its Members, as well as Defendants' Seizure of the Community's Tobacco Products (Counts VI and XIII).

Article II of the 1842 Treaty provides as follows:

> *The Indians stipulate* for the right of hunting on the ceded territory, with the other usual privileges of occupancy, until required to remove by the President of the United States, and *that the laws of the United States shall be continued in force, in respect to their trade and intercourse with the whites, until otherwise ordered by Congress*.

1842 Treaty, art. II (emphasis added). This provision remains in force and preempts Defendants from enforcing Michigan tax laws on commercial transactions by the Community and its members with non-Indians within the Ceded Area. The plain language of Article II establishes the preemptive purpose, meaning and scope of Article II, and the Court need not look further than that because "[i]f the treaty language is unambiguous, a court must construe the treaty in accordance with its plain meaning." *Yakama Indian Nation v. Flores*, 955 F. Supp. 1229, 1235 (E.D. Wash. 1997) (citing *Oregon Dep't of Fish and Wildlife v. Klamath Indian Tribe*, 473 U.S. 753, 774 (1985)).

Even if the meaning of Article II were not apparent from the plain text, any ambiguity would be resolved in favor of the Community. *Choctaw Nation v. Oklahoma*, 397 U.S. 620, 631 (1970). The words and actions of contemporary Indian Affairs officials show the preemptive purpose, meaning and scope of the Article II. First, the plain language of Article II requires the continued enforcement of all federal laws governing Indian trade and intercourse with non-Indians within the Ceded Area. At the time of the 1842 Treaty, the fundamental laws governing Indian trade and intercourse with non-Indians were collected and codified in the Act to Regulate Trade and Intercourse with the Indian Tribes, Pub. L. No. 23-161, 4 Stat. 729 (1834) (the "1834 Act"). Among other things, the 1834 Act required persons desiring to trade with Indians to be licensed and bonded; limited trading to locations designated by Indian Affairs officials; prohibited traders from obtaining guns, traps, utensils or clothing from Indians; and prevented anyone from selling or exchanging alcohol to or with an Indian within Indian country or otherwise introducing alcohol within Indian country. 1834 Act §§ 2, 7, 20; Nichols Decl. 31 (White Rpt.) at 5-6. Though Indian Affairs officials often expressed particular concern about enforcing the alcohol-related provisions of the 1834 Act within the Ceded Area, Article II plainly authorized enforcement of *all* provisions of the 1834 Act, and the Indian Affairs officials rigorously enforced nonalcohol-related provisions such as the licensing requirements within the Ceded Area. Nichols Decl. Ex. 29 (White Rpt.) at 5-7. Officials enforced within the Ceded Area all federal regulations and circulars relating to Indian trade and intercourse. *Id*. at 40, 45, 58.

Second, Article II *necessarily* requires the federal government to treat the Ceded Area *as if it were* Indian country in enforcing the federal Indian trade and intercourse laws within the Ceded Area. Because most provisions of the 1834 Act apply only to transactions within "Indian country," which is defined to exclude ceded Indian land, such provisions would not by their

terms apply to the Ceded Area. 1834 Act § 1. Prior to the 1842 treaty negotiations, chief negotiator Robert Stuart advised Commissioner of Indian Affairs T. Hartley Crawford that the United States should obtain cession of all the Indians' land, but that "[s]o much of the country should be reserved as Indian Territory, (so as to maintain the Indian laws &c.) for their use, as the President shall designate. . . ." Nichols Decl. 31 (White Report) at 16. Stuart did not use a presidential "reservation mechanism" in the 1842 Treaty to treat the Ceded Area as Indian country, but rather relied on the status of a treaty as the supreme law of the land to ensure that the federal Indian trade and intercourse laws continued to apply to the Ceded Area as if it were Indian country. Commissioner Crawford agreed with Stuart's approach, instructing Indian Affairs officials that the federal Indian trade and intercourse laws continued to apply in the Ceded Area as though Indian title had been retained, *i.e.* as though it remained Indian country:

> Your supposition in reference to the construction to be placed upon the 2d Art of the treaty is correct – the treaty is supreme and you will proceed against any offenders of the U.S. laws relating to trade & intercourse with Indian tribes in the same manner *as if the Indian title to the lands ceded have not been extinguished*.

Id. (White Rpt.) at 39 (emphasis added).

Third, Article II was understood by both Indian Affairs officials and opponents to preempt and displace inconsistent state laws. Accordingly, Indian Affairs officials excluded any introduction of alcohol into the Ceded Area, even though state law permitted such commerce. Indian Affairs officials also required each merchant that intended to trade with the Indians in the Ceded Area to post a bond and obtain a federal Indian traders license, even though state law permitted vendors to trade freely with Indians. *Id*. (White Rpt.) at 40. At the 1842 Treaty negotiations, Robert Stuart emphasized that pursuant to Article II federal Indian trade and intercourse laws would pre-empt state laws, noting that "[i]t will be better for you to have the same laws over you" (i.e. federal laws) "*than to have the laws of the states*." *Id*. at 20.

Opponents of Article II such as James Schoolcraft recognized and complained the Article II entailed federal preemption of state law, grumbling that Article II interferes with state rights and that "Michigan should be allowed to propose her own remedies" to the liquor issue. *Id*. at 27-28.

Fourth, by its plain language, Article II continued in force within the Ceded Area not only the 1834 Act but all future additions, amendments and extensions of the federal Indian trade and intercourse law. As Commissioner Medill declared in 1848, "all existing laws related to Indian Affairs are still in force" within the Ceded Area. *Id*. at 58. According to Defendants' putative expert Emily Greenwald, moreover, federal officials enforced within the Ceded Area an 1847 amendment of the 1834 Act, the Act of March 3, 1847, which prohibited the payment of annuities to Indians when the Indians were intoxicated or when, in the judgment of the local agent, intoxicating liquor was located close to the payment place. Nichols Decl. 32 (Greenwald Rbtl.) at 14-15. Dr. Greenwald strongly affirms that the federal Indian trade and intercourse laws addressed by Article II include future post-1842 laws, noting that "[s]ince 1842, the federal laws regarding trade and intercourse with Indians have evolved and changed. Article 2 did not require that the federal laws concerning trade and intercourse between Indians and non-Indians be frozen in 1842." *Id*. (Greenwald Rbtl.) at 29.

Fifth, Article II constituted an explicit and essential condition of the signatory Indian bands for making their land cession under the 1842 Treaty. Article II provides that "[t]he Indians stipulate" (1) "for" hunting rights and the usual privileges of occupancy in the Ceded Area, and (2) "that" the federal Indian trade and intercourse laws be continued in the Ceded Area. According to Merriam Webster, the verb "stipulate" means "to demand an express term in an agreement." Article II plainly identifies the Indians, not the United States, as the party that demanded the guarantees described in Article II. Because Article II immediately follows the

land cession described in Article I, the two guarantees described in Article II are presented as express conditions of the land cession. Robert Stuart confirmed this conclusion in 1843, asking with respect to Article II "had the Indians and the U.S. not a right to stipulate what the *conditions of sale* should be?" Nichols Decl. 31 (White Rpt.) 32-33 (emphasis added).

Sixth, Congress has never terminated the Article II. Article II was an express condition of the Indian signatories to the 1842 Treaty in exchange for ceding to the United States 10.5 million acres. As such, Article II constitutes a treaty-recognized right. The Seventh Circuit has expressly held that the first part of Article II, guaranteeing hunting rights in the Ceded Area, remained in effect because "a termination of treaty-recognized rights by subsequent legislation must be by *explicit* statement or must be *clear* from the surrounding circumstances or legislative history," neither of which requirements was satisfied. *Lac Courte Oreilles Band of Lake Superior Chippewa Indians v. Voight*, 700 F.2d 341 (7th Cir. 1983), *cert. denied*, 464 U.S. 805 (1983) (emphasis in original). The Supreme Court has subsequently stated that "Congress may abrogate Indian treaty rights, but it must clearly express its intent to do so." *Minnesota v. Mille Lacs Band of Chippewa Indians*, 526 U.S. 172, 202 (1999). The Court explained that:

> There must be clear evidence that Congress actually considered the conflict between its intended action on the one hand and Indian treaty rights on the other and chose to resolve that conflict by abrogating the treaty.

Id. at 203-04 (quoting *United States v. Dion*, 476 U.S. 734, 740 (1986)) (internal quotation marks omitted). No subsequent congressional statute or treaty even mentions Article II, much less terminates it.

Thus, Article II created a treaty-recognized right of the signatories and their successors to engage in commercial transactions with non-Indians in the Ceded Area under the jurisdiction of the federal laws governing Indian trade and intercourse. Those laws include the ones existing at

the time of the transaction, are enforced as if the Ceded Area was Indian country, and preempt inconsistent state laws to the extent permitted by existing federal law. The Sixth Circuit expressly confirmed these conclusions, quoting and approving the Western District of Michigan's conclusion that "the 1842 Treaty plainly makes federal law applicable to the Ceded Area, and federal law permits the states to impose their tobacco taxes on cigarette sales to nonmembers of the Tribe." *Rising*, 477 F.3d at 893. The Sixth Circuit confirmed that the federal Indian trade and intercourse laws apply to the Indians' transactions within the Ceded Area, that the Ceded Area is treated as if it were Indian country for purposes of enforcing such federal laws, and that the preemptive effect of such federal laws is governed by current federal Indian law, including case law, specifically citing the 20th Century case *Moe v. Confederated Salish and Kootenai Tribes of the Flathead Reservation*, 425 U.S. 463, 483 (1976), for the proposition that states can impose collection duties on Indians for sales to nonmembers. *Rising*, 477 F.3d at 893.

Because Article II requires enforcement of the existing federal Indian trade and intercourse laws within the Ceded Area as if it were Indian country, Article II has the following preemptive effects on Michigan law:

- **Michigan Sales Tax Act:** For the reasons stated above and in the First SJ Memorandum, Defendants are preempted by federal Indian trade and intercourse laws from imposing Michigan Sales Tax on purchases by the Community or its members within the Ceded Area, including the Reservation. Part I, *supra*; PageID.1616-19; 1622-26.
- **Michigan Use Tax Act:** For the reasons stated in the Community's First SJ Memorandum, Defendants are preempted by federal Indian trade and intercourse laws from imposing Michigan Use Tax on the use, storage or consumption of tangible personal property (and the housing or garaging of any motor vehicle) by the Community or its

members within the Ceded Area, including the Reservation. PageID.1616-19; 1622-26.

- **Michigan Tobacco Products Tax Act:** For the reasons stated above, Defendants are preempted by existing federal Indian trade and intercourse laws from imposing the Michigan Tobacco Tax with respect to purchases of tobacco by the Community or its members within the Ceded Area, including the Reservation. *Supra* at 23-41 (discussing the *Bracker* balancing test). In addition, Defendants are precluded by existing federal Indian trade and intercourse laws from seizing within the Ceded Area, including the Reservation, any tobacco product shipment addressed to or from the Community. *Supra* at 42-50 (discussing Indian tribal self-government and sovereignty).

CONCLUSION

For all of these reasons, this Court should hold that federal law prohibits enforcement of the Michigan Sales, Use, and Tobacco Tax Acts with respect to transactions by the Community and its members within the Reservation and Ceded Area, and grant the relief set forth in the Proposed Order submitted with this memorandum and incorporated herein by reference.

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Respectfully submitted,

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