

5-11-2006

Testimony on the Regulation of Indian Gaming, Oversight Hearing on the [NIGC] Minimum Internal Control Standards, Before the United States House of Representatives, Committee on Resources, 109th Congress, 2nd Session

Kevin Washburn
University of New Mexico - School of Law

Follow this and additional works at: https://digitalrepository.unm.edu/law_facultyscholarship



Part of the [Indian and Aboriginal Law Commons](#)

Recommended Citation

Kevin Washburn, *Testimony on the Regulation of Indian Gaming, Oversight Hearing on the [NIGC] Minimum Internal Control Standards, Before the United States House of Representatives, Committee on Resources, 109th Congress, 2nd Session*, (2006).

Available at: https://digitalrepository.unm.edu/law_facultyscholarship/525

This Court Filing is brought to you for free and open access by the UNM School of Law at UNM Digital Repository. It has been accepted for inclusion in Faculty Scholarship by an authorized administrator of UNM Digital Repository. For more information, please contact amywinter@unm.edu, lsloane@salud.unm.edu, sarahrk@unm.edu.



SCHOOL
OF LAW

SMALL SCHOOL.
BIG VALUE.

**KEVIN K. WASHBURN
ASSOCIATE PROFESSOR
UNIVERSITY OF MINNESOTA LAW SCHOOL¹**

**TESTIMONY
BEFORE THE COMMITTEE ON RESOURCES
UNITED STATES HOUSE OF REPRESENTATIVES**

**OVERSIGHT HEARING ON THE [NIGC] MINIMUM INTERNAL CONTROL STANDARDS
THURSDAY, MAY 11, 2006**

¹ The title and institution are provided for purposes of identification only. The views set forth herein reflect the views of an individual member of the legal academy and do not purport to reflect the official views of the University of Minnesota, its Law School, the State of Minnesota, or any other entity or person.

INTRODUCTION

Because Indian gaming is one of the most important sources of revenue for many Indian tribes, it is crucial that the industry remain well regulated. Strong regulation serves several practical functions. First, it protects Indian gaming from crime, ranging from petty theft by low-level employees to complex money laundering activities by members of organized crime. Second, strong regulation provides comfort to the gaming patron and the public in general that gaming is being done in a fair and honest manner and is free of criminal influence.

The particular vulnerability of gaming is that casino gaming involves large sums of cash changing hands in millions of transactions each day by thousands of people across the country. In an age in which transactions in most other areas of commerce are dominated by less fungible and more secure financial instruments, such as credit cards, debit cards and checks, casinos still predominantly operate with cash. The cash intensive nature of the gaming industry makes it particularly attractive – and particularly vulnerable – to crime and corruption.

Despite this vulnerability, crime and corruption has, for the most part, been controlled in Indian gaming through vigilant adherence by gaming regulators to two primary regulatory strategies: careful background investigations of the key actors in Indian gaming, and strong internal control procedures for casino operations. It is widely agreed within the gaming industry in general that background investigations and internal controls are crucial to effective regulation. Today, no reasonable commentator could seriously deny the importance and effectiveness of these regulatory strategies in protecting the industry.

Thus, the key question today is not whether these regulatory strategies are valuable and important, but which governments, tribal, federal, or state, should bear the ultimate responsibility for implementing these regulatory strategies. The regulation of gaming has been plagued by a lack of clarity in the roles of the respective regulatory entities. It is an appropriate time for Congress to clarify those roles to provide better guidance to the industry and to gaming regulators.

A. THE ROLE OF STATE GOVERNMENTS IN REGULATING INDIAN GAMING.

When IGRA was enacted in 1988, most observers anticipated that states would take the opportunity afforded by the tribal-state compacting process to develop a strong regulatory presence over Class III Indian gaming. Some states took that opportunity and developed strong, reliable, and effective gaming regulatory agencies that provide vital assistance in insuring the integrity of Indian gaming. Other states, however, expressed little interest in regulating Indian gaming and failed to negotiate a significant regulatory role in tribal-state gaming compacts. These states have been “no-shows” in the important area of

regulation. While substantially all of the states have shown a strong interest in tribal gaming revenues, fewer have shown significant interest in the actual regulation of Indian gaming. In other words, state gaming regulation has been inconsistent: strong in some states, weak in others.

Even in the states that have undertaken a significant regulatory role in Class III Indian gaming, their efforts are vulnerable to criticism. Some of these criticisms are in the nature of conflicts of interest. On one hand, a state may feel ambivalent or even somewhat hostile to Indian gaming activity. For the Indian tribes that have gaming operations, gaming revenues help them maximize the exercise of their tribal governmental power and authority, that is, their tribal sovereignty. American history is littered with clashes between states and tribes; American legal history is a reflection of these battles. A leading Supreme Court case once described the people of the states as “the deadliest enemies” of American Indian tribes. While today these clashes are less often “deadly” in the most immediate sense, the clashes between tribal and state authority continue. Indeed, in recent years, one such clash or another has gone all the way up to the Supreme Court nearly every Term. In this context, it is easy to see why state governments may feel conflicted about preserving the integrity of Indian gaming to help tribes maximize tribal sovereignty.

On the other hand, where a state government does have an interest in maximizing Indian gaming revenues, which occurs when tribes have entered gaming revenue-sharing arrangements with state governments, states may have a different sort of conflict of interest. States that share Indian gaming revenues have an interest in maximizing gaming revenues. Meeting strict regulatory requirements can sometimes be expensive; compliance can therefore affect the bottom line and reduce gaming profits. A state’s short-term interest in maximizing revenues may therefore overshadow its interest in the integrity of Indian gaming. This can also create a potential conflict of interest for state regulators.

As a result of these conflicts of interest at the state level, state regulation leaves the Indian gaming industry vulnerable. The quality of regulation of Indian casinos ought not be subject to the mercy of state budgetary cycles or vary because of a potential conflict of interest. Congress should respect the decision of some states to “opt out” of Indian gaming regulation. That does not mean, however, that Indian gaming should be left unregulated if a state refuses to undertake this important responsibility. The federal and tribal governments must exercise appropriate roles over Class III gaming, and Congress should clearly recognize those roles. The integrity of Indian gaming must be carefully protected if Indian gaming is to remain an important tribal asset in the future.

B. THE PROPER ROLE OF TRIBAL AND FEDERAL REGULATORS IN INDIAN GAMING.

1. Tribes should have the primary responsibility, though not the exclusive responsibility for regulating Indian gaming. The primary responsibility for insuring that Indian casinos adopt and adhere to adequate internal controls ought to lie with tribal gaming regulators who have the advantage of physical proximity and already exercise a variety of regulatory functions within Indian gaming operations. During the past fifteen years, a large and sophisticated community of professional tribal gaming regulators has taken root across the country. Tribal gaming regulators have proven themselves, in the main, as effective regulators. In most circumstances, tribal regulators work conscientiously, competently and independently in providing strong regulation of Indian casinos. Recognizing their primacy in undertaking these sovereign responsibilities is likely to produce the most effective regulation. However, tribal regulatory structures have some obvious regulatory weaknesses and vulnerabilities that justify a strong oversight role for federal regulators, including the need for federal regulators to take independent enforcement action where tribal gaming regulators fail to meet their sovereign responsibilities.

2. Each tribal regulator has a responsibility to his own tribe that makes him myopic as to the national interest of all Indian tribes. Federal regulators, on the other hand, can protect the integrity of the entire industry. Although it is true that fundamental notions of tribal sovereignty and self-determination ought to protect the right of each tribal government to make regulatory decisions without federal oversight, Indian gaming is an exception to this principle. I justify exceptionalism on this basis: one of the practical ramifications of tribal sovereignty is that no tribe can be held accountable to any other tribe. Yet, despite their legal insulation from one another and their lack of mutual accountability, Indian tribal decisions can harm other tribes. In the highly politicized world of Indian gaming, no tribe is an island unto itself. Indeed, the political fallout from incompetent or corrupt actions of one tribe may well impact hundreds of other tribes across the country. Indian gaming exists at the sufferance of Congress and state legislatures and the public whom those bodies represent. If one tribe's casino succumbs to corruption or otherwise earns infamy, then the entire Indian gaming industry may well be tainted. The integrity of the industry – and even the *perception* of integrity – must be guarded with vigilance. In Indian gaming, tribes are linked inextricably to one another. Because no tribe has the ability to regulate other sovereign tribes, this problem is one that tribes cannot solve themselves. In my view, this lack of accountability of one tribe to another justifies federal oversight to accomplish what tribes cannot achieve through collective action. In other words, the federal government's own sovereign authority in this area can offer sound regulatory coverage that tribes could never achieve on their own.

3. Federal regulators can provide oversight to tribal regulators, who may have conflicts of interest, and may need external support to buttress their authority within the tribal government. The risk of occasional irresponsible behavior by tribal regulators is quite real, for a couple of reasons.² First, the Indian Gaming Regulatory Act does not currently require that Indian tribes have independent tribal gaming commissions. Many tribes have created gaming commissions, but the relative independence of these commissions varies. Tribal commissioners are sometimes directly accountable to tribal leaders and/or tribal voters. While, in most circumstances, the tribal interest in the long term health of the gaming operation will give each tribal regulator a strong incentive to regulate responsibly, there may occasionally be overwhelming temptation to cut regulatory corners for short term gains. In other words, tribal regulators have the same type of conflict of interest that state regulators have. And, in some cases, the conflict will be even more severe. Federal regulators can minimize the damage caused by such conflicts of interest by subjecting tribal regulators to independent oversight.

4. Tribal regulators will sometimes lack the will to close an Indian casino that has engaged in gross irregularities. Because most tribal governments operate only a single Indian casino, and thus the tribal gaming regulatory agency has authority only over one casino, there is a serious risk that the tribal regulator will occasionally “pull his punches.” In circumstances where one tribe operates one casino, the tribal regulator’s job is dependent on the existence of the Indian casino. Such a regulator will not be inclined to shut down the casino even for gross misconduct. Hopefully, the need for closure of an entire casino will be rare, but it is precisely in the most egregious circumstances when it ought to be done. The NIGC must have clear authority to take appropriate action over Class III casinos, including closure, especially in cases in which tribal regulators fail to act.

5. Tribal regulators are also more likely to succumb to “regulatory capture.” “Regulatory capture” is the term used to define a regulatory agency’s tendency to align its interests and collude with the firms it is ostensibly regulating, to the detriment of the public interest. The rich and diverse academic literature on capture reflects the notion that a regulated industry will attempt influence the regulator to prevent vigorous enforcement of the regulatory regime. Some scholars say “capture” is unavoidable: regulators will become instruments of the regulated community and will inevitably act in favor of the regulated community. Others take a pragmatic view that “capture” will exist to a greater or lesser degree depending on the legal structures that are used to guard against it, but that the threat of capture can be managed with prudent laws and sound regulatory structures. One risk factor for capture is a high degree of discretion by regulators. Wide discretion not only creates the opportunity for regulators to rule in favor of the regulated community, but also provides cover for doing so because the essence of discretion is power unconstrained by enforceable legal authority. The regulation of

² I addressed some of the same issues in detail in testimony before the United States Senate Committee on Indian Affairs on April 27, 2005, and September 21, 2005. A link to this testimony can be found at <http://www.law.umn.edu/facultyprofiles/washburnk.htm>.

gaming almost always involves a high degree of discretion by regulators. Many regulators assert as a matter of law that their discretion to grant or deny gaming licenses is unfettered by due process requirements because involvement in gaming is not a right, but a privilege. Though this argument is less compelling under modern notions of due process, it reflects a widely held view among gaming regulators and it creates enormous unchecked discretion in the hands of the gaming regulator. Such broad discretion can increase the risk of capture.

6. Federal regulatory oversight can minimize “capture” of tribal regulators. Another risk factor relates to the number of groups interested in the regulator’s performance. A regulatory agency that has many regulatory entities within its jurisdiction and many other interested groups interested in its work is less likely to succumb to capture by any one group, because it will be held accountable to some degree by each of the entities and interested groups and each will scrutinize agency action. So, for example, when the FCC makes a decision related to the regulation of communications, AT&T or Verizon may cry foul if Qwest gets favorable treatment that the others perceive as unfair. Such competition within the regulated industry makes the regulator more accountable and thus serves as an important check on regulatory capture. In contrast, many tribal regulatory agencies have authority over only a single entity. In this “one tribe, one casino” model, tribal regulators work repeatedly with the same Indian casino officials. Thus, the structure of Indian gaming markets renders tribal gaming regulators tremendously vulnerable to capture. Tribal regulators will thus face less scrutiny than other regulators; they will hear only one voice, rather than many, when they make regulatory decisions. While outside interest groups can sometimes have an impact in preventing capture, there are few independent interest groups looking out for tribal members or casino patrons in the Indian gaming industry. Federal regulators can serve the role of overseeing tribal regulators, pushing them to be vigilant and requiring them to resist capture.

7. Federal regulators have a comparative advantage in protecting all Indian gaming. Because of internal tribal pressures and the natural conflicts of interest of tribal regulators, federal regulators have a comparative advantage. Federal regulators are largely disinterested and objective; they have no significant conflicts of interest because they obtain no direct or significant benefit from the development of any particular Indian gaming facility.

8. Uniform federal standards are better than individual state or tribal standards because federal standards can assure the integrity of gaming on a national scope and indirectly increase the quality and independence of tribal regulators. In the context of internal controls, the adoption of uniform federal standards creates a baseline for quality of regulation nationwide. Creation of such standards not only helps patrons, it facilitates the independence of tribal gaming commissioners by insuring that knowledge and expertise is portable from one reservation to another. Nationwide standards assure a national network of training and job opportunities that collectively serve to improve the professionalism of tribal gaming regulators. If a tribal regulator is fired from one

reservation for applying the rules too rigorously, for example, he may well be able to find work with a gaming commission at another reservation.

9. Federal regulation is best if it allows adequate flexibility at the tribal level. Federal regulators cannot be as responsive to the unique needs and circumstances of each individual tribe. Moreover, technology and other relevant circumstances will change much more quickly than regulators can update a complex and comprehensive regulatory regime, such as the federal minimum internal controls standards. To address these disadvantages, tribal gaming commissions and federal regulators should be open-minded and sensible about allowing reasonable variances to the federal standards.

C. RECOMMENDATION

Indian tribes deserve clarity about the gaming regulatory structure. Likewise, the NIGC will be able to operate with greater confidence and legitimacy if it has a clear Congressional mandate on its authority to regulate. Because it is in the best interest of Indian gaming for an independent and objective regulator to oversee all significant gaming activity, Congress should strengthen the NIGC's mandate over Class III gaming. **Congress should recognize the NIGC's authority to assure the integrity of Indian gaming extends to Class III gaming activity for all purposes, including background investigations of management contractors, minimum internal control standards, and health and safety.**

Second, federal Indian gaming regulators must be cognizant of the fact that it is sovereign *governments* they are regulating. Many disputes between Indian tribes and the NIGC have arisen when federal regulators have behaved in a heavy-handed fashion. While such heavy-handedness is the norm among regulators within the commercial gaming industry in Nevada and New Jersey and other jurisdictions, the circumstances are far different in Indian gaming. Regulators in Nevada and New Jersey are regulating private actors, not sovereign nations.

Federal regulators must behave much more carefully and respectfully toward the regulated industry. **To be effective, NIGC regulators must not be merely regulators, but also educators and diplomats.** While federal regulators must utilize a variety of skills to achieve tribal compliance, reliance on aggressive regulatory tactics sometimes simply masks ineffectiveness. Federal regulators should treat tribal regulators and tribal officials with the same respect and deference that they would use toward state officials. To some degree, this means that the NIGC requires adequate financial resources to recruit, hire, and retain the best regulatory professionals in the country. Given the context, the task for federal regulators is simply much more difficult than for state regulators.

CONCLUSION

To protect the value of Indian gaming as a resource for all tribes, Congress should clarify the strong role for federal regulators in Class III Indian gaming. For most tribes, which engage in responsible regulation of Indian gaming, the NIGC role will be nearly invisible. While a strong role for the NIGC clearly treads on tribal sovereignty, it is a pragmatic and necessary step to insure the long-term viability of gaming as a resource for all tribes.

Thank you for seeking for my views on this important subject.

Kevin K. Washburn
Associate Professor
University of Minnesota Law School
229 19th Avenue South
N226 Walter Mondale Hall
Minneapolis, MN 55455

email: kkw@umn.edu
phone: 612-624-3869
fax: 612-625-2011

<http://www.law.umn.edu/facultyprofiles/washburnk.htm>