

National Indian Gaming Commission
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Oversight Field Hearing
Northeastern Oklahoma A & M College
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Good morning Congressmen Boren and Cole and members of the Committee.

My name is Philip Hogen, and I am a member of the Oglala Sioux Tribe from South Dakota. I have had the privilege of Chairing the National Indian Gaming Commission (NIGC) since December of 2002. Currently the NIGC has two Commissioners, myself and Vice Chairman Norman DesRosiers, who is here with me today. Thank you for the opportunity to testify about regulations affecting economic development in Indian Country.

In the late 1970's and early 1980's, Indian tribes began to employ bingo and some other forms of gambling as an economic development tool. Despite challenges from some state governments and elsewhere, this tool proved successful. Following an era of litigation, Congress brought some finality to the structure of Indian gaming with the enactment, twenty years ago, of the Indian Gaming Regulatory Act (IGRA), rightfully reciting a principal purpose of enhancing economic development for Indian tribes.

Among other things, Congress created the National Indian Gaming Commission (NIGC) to promulgate federal standards to implement the IGRA, and to provide some federal oversight of that Indian gaming. NIGC's role, then, is to foster the economic development IGRA intended. This is best done by ensuring that there is integrity in the operation and regulation of tribal gaming and that fidelity to the language and spirit of IGRA is maintained.

What is abundantly clear to me from a study of IGRA's language and legislative history is that Congress intended to distinguish between Class II and Class III gaming. Class II games may be played with electronic aids and require no compact with the state; Class III games include electronic facsimiles and can be played only pursuant to a compact with the state. However, evolving technology-- not known at the time of IGRA's adoption-- has clouded the distinction between the two classes of gaming. So long as there is confusion between what constitutes Class II games played electronically and Class III games that require compacts, the long-term success of economic development for tribes through gaming will be threatened. Tribes that cannot distinguish the two risk installing machines that will later be subject to enforcement actions or criminal sanctions. More ominously, operating as Class II games that are properly Class III has the potential to attract a legislative effort by the Congress to curtail Indian gaming or greatly expanded commercial competition from the states, something we are already beginning to see. This is what we are striving to avoid. NIGC has thus promulgated a set of regulations with which it intends to bring needed clarity to this issue and thus to ensure Indian gaming's long-term success while maintaining the distinction mandated by IGRA's statutory language.

Recent Historical Background

The present regulatory effort did not arise out of nothing. Rather, it arose against a background of a proliferation of uncompact Class III games here in Oklahoma. In January of 1999, Montie Deer, my predecessor as NIGC Chairman, began a series of enforcement actions in an attempt to halt this spread. He was successful to a large extent. Most tribes ceased operating uncompact Class III games in the face of NIGC enforcement. Some tribes, however, continued to play uncompact games. With those tribes, NIGC engaged in protracted administrative litigation – for the tribes, an expensive proposition in its own right – and at the end of that litigation, some tribes had their gaming operations shut down, received multi-million dollar fines, or both. The burden of the illegal activity fell upon the tribal membership, the very people whom IGRA was designed to help. In that sense, then, the enforcement actions were not a success.

When I became NIGC Chairman, I picked up the process of bringing enforcement actions against uncompact Class III games where Chairman Deer had left off. After a time, however, I realized that the effort was unsuccessful in another way. By its nature, the enforcement actions were brought against a particular tribe for playing particular uncompact Class III games. I discovered that after all of the litigation was said and done, as soon as NIGC succeeded in demonstrating that a particular machine was in fact a Class III gambling machine, a machine with similar operating characteristics but a different name and cosmetic appearance would show up, and we would have to begin all over again with expensive and time consuming litigation. This employed lawyers, but it didn't help the tribes. The solution, then, not only for fencing out uncompact Class III games but also for providing a clear dividing line between Class II games played with electronic aids and Class III facsimiles is a uniform set of standards that would have nationwide application and upon which tribes could rely when choosing which machines to place in their gaming operations.

Regulatory Approach

In writing and proposing the proposed classification rule, the Commission has been mindful of the language of IGRA, Congress's intent, IGRA's legislative history, relevant court cases, and the essential need of the tribes for a broad, flexible and legally sustainable scope of Class II gaming. Class II was the basis on which Indian gaming was built. Since the enactment of IGRA in 1988, Indian gaming has grown into a \$26 billion business, far eclipsing the industry that Congress could have envisioned. Although an estimated 90% of this gross gaming revenue is generated by compacted Class III gaming, Class II remains significant to tribes throughout the country.

Tribes play Class II games for a variety of reasons. For some tribes with Class III gaming compacts, Class II is a vital supplement, long enjoyed and preferred by some clientele. In other cases, some states refuse to compact with their tribes for Class III play, even though they allow Class III gaming activities elsewhere within those states or tolerate wide-spread illegal Class III activities in non-Indian gaming facilities. Tribes in that situation are left to make the most of Class II gaming and have operations that are, or

were, places where the distinction between Class II and Class III has become the most blurred and where clarity is most needed. Further, as tribes negotiate with states for Class III compacts, they and the states need to know that there are viable Class II games that tribes may utilize if no agreement is reached.

Unfortunately, the statutory language of IGRA lacks clarity when it makes “computer and electronic and technologic aids” Class II but places “electronic facsimiles of games of chance” in Class III. However, some of the IGRA’s legislative history sheds light upon Congress’s intended goal.

In the House and Senate floor debates, several proponents of the legislation described the distinction as that between “bingo” (Class II) and “casino gaming” (Class III). While “casino gaming” likewise lacks a crystal-clear definition, those who spoke associated the term with gambling halls filled with slot machines, venues separate and distinct from the bingo halls of the 1980’s.

It further appears from the debates that a basis for making this the dividing line between Class II and Class III was the complexity and regulatory difficulties associated with slot machines and casino gaming. Some argued that only states— then the only governments experienced with the conduct and regulation of such activity—were up to the task of regulating casino gaming, and thus casino gaming needed to be compacted.

Much has changed, of course, since those debates in 1988, not the least of which is the sophistication and excellence of the tribes’ own gaming regulation. Tribes spend hundreds of millions of dollars annually regulating their gaming, both directly through their own commissions, and indirectly by funding the regulation done by states and the NIGC. Nonetheless, the distinctions and classifications established in IGRA in 1988 still bind the Commission, and the proposed rules seek to identify and clarify the line Congress intended to draw between Class II and Class III. I believe that if that line is not clear and identifiable, Congress’s intent will not be fulfilled.

Since IGRA’s adoption in 1988, the world has changed, and computerization has transformed whole sectors of our economy and society, including gaming. These

technological advances challenge the legislative language that pre-dates them. Nevertheless, the language of IGRA continues to govern Indian gaming today. Unless or until that language or the mission of the NIGC—in part to promulgate standards for Indian gaming—is changed, the Commission’s must uphold that language.

IGRA is not the only legislation governing Indian gaming. The other legislation, of course, which applies to the use of gambling equipment on Indian lands, is the Johnson Act. Since it was enacted in 1953, the Johnson Act has provided that there could be no “gambling devices” in Indian Country, and the term “gambling devices” has been broadly interpreted.

The passage of IGRA in 1988 changed this in two ways. “Gambling devices” could be used on Indian lands if they were used pursuant to Class III tribal-state compacts, and tribes could use computers and electronic and technologic aids in the play of Class II bingo and similar games.

And so developed different interpretations of what constituted “gambling devices” and “technologic aids.” When electronic and technologic features were introduced in the absence of a tribal-state compact, some federal investigators and prosecutors saw “gambling devices.” This view was upheld when the Ninth Circuit held that an all-electronic form of pull tabs to be an electronic facsimile game of chance, notwithstanding the argument that players were playing against other players and not against the machine they were using. The electronic replication of the traditional Class II pull tab game was deemed a Class III electronic facsimile and hence prohibited on Indian lands in the absence of a compact. See Sycuan Band of Mission Indians v. Roach, 54 F.3d 535 (9th Cir. 1995).

By contrast, in a series of decisions involving an electronic bingo game called MegaMania, courts considered electronic, computerized player stations, which interconnected a minimum of 12 players and displayed bingo cards and bingo balls to them. Each game took from two to three minutes to play. Again, those responsible for enforcement of the Johnson Act challenged the player stations as “gambling devices”

requiring a compact for play. These challenges failed. Accordingly, the player stations were indeed only “aids” to the play of bingo, which Congress provided for in IGRA as Class II, and not electronic facsimiles of a game of chance. Those courts, however, were careful to note that their conclusions were limited to the facts of the cases presented. See U.S. v. 162 Megamania Gambling Devices, 231 F.3d 713, 725 (10th Cir. 2000), U.S. v. 103 Electronic Gambling Devices, 223 F.3d 1091 (9th Cir. 2000).

Similarly, in a series of cases dealing with dispensers of paper pull tabs known as Lucky Tab II and Magical Irish, the enforcers of the Johnson Act became concerned when the manufacturers of these machines added video displays to the machines. The displays interpreted winning and losing pull tabs by depicting slot machine-type reels and showing winning and losing combinations. These dispensers, it was said, were “gambling devices” and could only be played in a compacted Class III arrangement. The courts disagreed. Notwithstanding the use of the entertaining displays to show slot machine-like results, those displays were not essential to the game. The play of the game was “in the paper” – it was the pull tabs themselves, and only the pull tabs, that determined the outcome of the game. Thus, these courts concluded, the electronic dispensers were only aids to the play of the game of pull tabs and permissible without a Class III compact. Again, the courts limited their holdings to circumstances before them. See Diamond Game Enterprises v. Reno, 230 F.3d 365 (D.C. Cir. 2000), Seneca-Cayuga Tribe of Okla. v. NIGC, 327 F.3d 1019, 1031 (10th Cir. 2003).

Thereafter, these technologies—interconnected bingo player stations and slot machine-type video displays (not determinative of results)—were coupled, and currently most electronic bingo systems employ such technology. Most such systems display the results of the bingo game in an electronic bingo card on the equipment’s video display.

Such technological advances have greatly increased the speed with which bingo is played and have made the experience of playing very similar to the experience of playing conventional slot machines. In adopting IGRA, Congress observed that while computers, electronic and technologic aids may assist the play of Class II games, a Class III facsimile results if those electronic aids incorporate all of “the fundamental characteristics” of the

Class II games. This, the Commission believes, is precisely the issue raised by the proliferation of so-called “one touch games” -- inter-connected electronic bingo player stations with which players initiate and complete play of a bingo game with the single touch of the screen or a button. Such games are why the Commission has issued the proposed rules: to make clear that the play of a Class II bingo game with technologic aids differs from play of a Class III slot machine.

In such instances, the equipment has ceased to be an “aid” to the play of the game, and has become one of those “electronic facsimiles of games of chance” which Congress placed in Class III. When the equipment automatically, electronically automates the play of the game and the players’ participation in the game, the Commission believes that the play is no longer “outside” the equipment and that the electronic equipment can no longer be characterized as merely an aid. All player attention, discretion, and interface have been automated by the equipment.

Beyond this, the full electronic automation of bingo creates distortions in the way bingo is played. There is considerable significance to being the first player to “win” the bingo game by getting a “bingo” or the game-ending pattern. Many current, fully electronic games, however, often place minimum significance on this important characteristic of bingo and rather award the principal prizes to interim or consolation patterns and winners. There is less competition among players -- a fundamental characteristic of bingo -- for these interim prizes than there is for the game-ending prize. If multiple players hit the game-ending prize simultaneously, the common practice is to split the prize among them. By contrast, it is often the case that players who hit interim prizes are awarded the full prize, without regard to the number of other players who have also hit it.

Economic Impact

Finally, I would like to say a few words about the economic impact study the Commission released to the public at the beginning of this month. In particular, I'd like to address what the study is and what it is not.

When we first started this exercise three and some years ago, we did not foresee a large economic impact. After we proposed our first set of classification regulations in May of 2006, however, a number of commenters asked us to take a specific look at the economic impact of the proposed rules because they thought it would be considerable. We agreed and contracted with an economic analyst to evaluate the economic impact of the proposed regulations. We published the analyst's report in November of 2006. The size of the economic impact was one of the reasons the Commission withdrew that first set of proposed rules. When we published the current proposed rules in October of 2007, we commissioned an update of the previous economic study, and that update is what we published this month.

The study attempts to quantify the economic impact of the proposed classification and technical standards on a national level. As the Committee is aware, and as the study itself says, there is a tremendous diversity in Indian gaming. There is a diversity in the size of operations, in their geography, in games they offer, and in the political acceptance with which they are greeted by state and local governments.

Thus, the study, by design, does not attempt to "drill down" and measure the economic impact of the proposed rule at the local levels, for to do so nationwide would be prohibitively time consuming and expensive. To measure the impact on local communities in Oklahoma, where there are many gaming operations, where some are close by one another, and where the tribes have compacted with the state and thus have the option of switching to Class III games, would be an analysis unto itself. That analysis would be quite different than the analysis for tribal gaming in Alabama, where there is no compact and no current Class III option, where there is little Indian gaming, and where commercial gaming is a direct competitor. In turn, economic effects in Oklahoma and Alabama will be different than effects in South Dakota, where compacts strictly limit the number of gaming devices a tribe may employ; in California, where compacts just

approved will allow for thousands more slot machines; and in Alaska, where everything is remote.

That said, I would note that the tribes in Oklahoma are insulated from the danger of losing gaming revenue under the proposed rules in ways that tribes in some other states are not. As the economic study states, the tribes in Oklahoma now have a more-than-viable alternative to Class II gaming because, since November 2004, they have had the ability to enter into compacts with the State and offer Class III slot machines for play. In fact, the tribes, irrespective of our classification efforts I believe, have been moving full steam ahead toward Class III gaming. We understand from the State of Oklahoma that by the end of 2007 the tribes were operating over 25,000 compacted electronic games, approximately half of the electronic devices in the state – and that up from nothing just two and a half years ago.

In any event, Class III slot machines earn more than Class II games do industry-wide. In Oklahoma, the economic impact study finds that Class III games, on average, earn \$145 per day and Class II games \$125. That \$20-a-day difference is significant. Our own calculations show that a tribe that converts 20% of its Class II games to Class III games each year for the next five years will be millions of dollars ahead, even counting the retail cost of new equipment and additional revenue sharing with the State.

In this same vein, I would venture to say also that a large percentage of the economic loss predicted by the economic study may already be moot. The study reports that California, Florida, and Oklahoma account for approximately 84% of all Class II machines in play.

Four of the six tribes in California that operate approximately 75% of the Class II machines in that state have new compacts that allow them 17,000 additional Class III machines, and they are rapidly replacing their Class II machines with the machines. In Oklahoma, as I just noted, Class III games make up half of the machines in the state, with only more to come. In Florida, the recently compacted Seminole Tribe is rapidly replacing its 8,615 Class II machines with Class III machines.

From this, one can reasonably conclude that within a reasonably short time, over 50% of the adverse economic impact cited in the study will be mooted. In fact many of the tribes in the states cited above will enhance their economic status by moving from Class II gaming to Class III devices.

All of this is not to say that the Commission is not interested in local effects. To the contrary, the more information we have about these proposed rules, and the more comments we receive, the better able we are to make an informed decision about them. If any representatives of local government here, or elsewhere in the country, wish to provide us with information we do not have, we welcome this. The comment period for the proposed rules is open until March 9, 2008.

Finally, this economic study is not the end of our process and not the end of the consideration the Commission is giving to the economics of the proposed rules. Rather, the study is a necessary step along the way to a final decision. Now that we know the proposed rules will have a significant economic impact, we are obligated by law to undertake a cost-benefit analysis of them. We are in the process of contracting for that now. That study will, as its name suggests, examine both the costs and the benefits of the proposed rules. That study, together with this economic study and all of the comments we have received and will receive, will all inform the Commission's final decision about these proposed rules. Our minds are not made up. We have listened to all of the comments we have received in this long process, and we will continue to do so.