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Statement of Philip N. Hogen Chairman, National Indian Gaming Commission

Committee on Senate Indian Affairs

April 27, 2005

Good morning Chairman McCain, Vice-Chairman Dorgan, Members of the Committee and Staff. My name is Philip Hogen. I am the Chairman of the National Indian Gaming Commission ("NIGC") and a member of the Oglala Sioux Tribe of the Pine Ridge Indian Reservation in South Dakota. Seated with me today are Commissioners Nelson Westrin, a former Executive Director of the Michigan Gaming Control Board, and Cloyce "Chuck" Choney, a member of the Comanche Nation of Oklahoma and former Special Agent for the Federal Bureau of Investigation.

I'm very pleased to bring you a report of the activities of the NIGC and its efforts to fulfill the role assigned it under the Indian Gaming Regulatory Act ("IGRA"), and to address the concerns that Congress expressed in IGRA regarding the operation and regulation of gaming on Indian lands.

In general, the health of the Indian gaming industry provides profits and opportunities for economic growth in Indian country. There continues to be a steady increase in the revenues generated by over 400 tribal gaming operations, operated by more than 225 gaming tribes in 28 states. While only some gaming tribes have become wealthy, tribes that conduct gaming are able to provide jobs to run the operations and governmental programs with the revenues generated. These revenues fund tribal programs, strengthen tribal governments, promote and diversify economic development on those tribes' reservations, and address many needs that were not addressed before the advent of Indian gaming. Certainly, Indian gaming has not resolved all of the economic challenges in Indian country, but I believe it has been the most effective tool that tribes nationwide have yet employed to seek, and in a number of cases achieve, self-sufficiency, and, of course, to promote self-determination and strengthen tribal sovereignty.

Like all other market-oriented enterprises, Indian gaming has been, and will continue to be, most successful in those areas where there is ready access to population centers and where the mar-

ket for gaming opportunities has not been saturated. Unfortunately, many tribes are located remotely from such markets and likely will never be able to rely on gaming for economic development in a large way.

One of the keys to the significant success Indian gaming has enjoyed has been the perception, and the reality, of adequate regulation. This regulation is first and foremost provided by the tribes themselves by way of their tribal gaming commissions and gaming authorities. Where tribes have entered into compacts for Class III gaming with the states in which they are located, regulatory tasks have been shared, to one degree or another, by the state governments with whom the tribes have compacted. There is great diversity with respect to the extent of the states' roles, and it is difficult to generalize with respect to the extent and nature of states' regulatory involvement in tribal gaming. Suffice it to say, many tribal-state compacts provide for very limited state regulatory involvement regarding Class III tribal gaming.

The economic miracle that Indian gaming became for many tribes in the late 20th century, and continues to be as we enter the 215' century, is rightfully attributed to the initiative, creativity and resourcefulness of the gaming tribes.It might be said that this success was achieved in spite of restrictions which IGRA imposes. But no small part of this success is attributable to the fact that Indian gaming was required to be, and is, thoroughly regulated. In particular, IGRA's direction to the NIGC to provide federal regulatory oversight and to develop, promulgate and administer federal standards significantly contributed to that regulatory effort and the related success of Indian gaming. I don't mean to assert that Indian gaming is successful solely because of the NIGC's regulatory role, but I don't think it can be fairly said that its success was achieved in spite of the NIGC's regulatory role.

Under IGRA, the NIGC was tasked with providing an oversight regulatory role, and the Commission continues to strive to effectively provide that oversight and not be more intrusive than necessary. We strive to be efficient and avoid duplicating regulation that the tribes, and in some cases the states, already adequately provide. In particular, where the tribes and states have agreed to specific regulatory standards in their compact, we defer to the compacted standards. However, where the compact is silent, we have followed Congress' direction to promulgate and implement minimum federal internal control standards necessary to ensure adequate regulation and control and to carry out the provisions of the Act and accomplish its purposes.

RESOURCES FOR FEDERAL OVERSIGHT OF TRIBAL GAMING

As you know, the NIGC has not received an appropriation of tax payers' dollars to fund its operations since 1998. Rather, the NIGC's operations are funded solely by the fees, authorized under IGRA, assessed on the tribes' gaming revenues. As authorized by the Interior Appropriation Act of the 108th Congress, the amount of fees the NIGC may assess and collect may not exceed $12 million annually. While the industry has grown, and the needs of the NIGC for resources to provide oversight have similarly grown, the NIGC was able to fund its role with an expenditure of $10.4 million in 2004 (calendar year), and contemplates that it will be able to adequately fund oversight of the growing industry in 2005 and 2006 within its current $12 million assessment cap.

A general breakdown of the NIGC's past and projected expenditures is set forth in the following table: The NIGC, like most regulatory agencies, expends most of its budget to compensate its personnel. There are currently 78 individuals employed by the NIGC. The breakdown of personnel is as follows:

The rate for the fee assessments is established annually by the NIGC, based upon aggregate tribal gaming revenues nationwide. The NIGC has established a preliminary assessment rate of

.059% to fund the current year's operations, based on 2004 tribal gaming revenues. A final rate will be established after all 2005 revenues are calculated.

The following chart demonstrates the rate the NIGC has assessed tribes in years past:

The declining rate has been made possible by the fact that tribal gaming revenues continue to grow at a healthy and steady pace. The following table reflects the growth of gaming revenues in the last several years.

CHALLENGES TO NIGC OVERSIGHT

There will always be a dynamic tension between the regulator and the regulated community, and this is and has been true of the NIGC and the Indian gaming community. It is my perception that there is a growing feeling among some gaming tribes that the yoke of federal oversight, as structured in IGRA, ought to be thrown off, and I am concerned about this trend. Tribes should and do stand up for their sovereignty, and they should resist unmerited intrusions into their affairs. As Indian gaming is now successfully conducted, however, it is within the carefully crafted framework established by IGRA. If this structure becomes unbalanced, the success it has enjoyed is placed at risk. A manifestation of this trend, in my view, would be widespread tribal support for current litigation which challenges application of the NIGC's Minimum Internal Control Standards to Class III gaming activities. In my experience, the Minimum Internal Control Standards have been the single most comprehensive and effective tool the NIGC has developed to ensure consistent quality operation and regulation of gaming activity on Indian lands, and, of course, the vast majority of tribal gaming activity and revenues occur within Class III gaming. Similarly, tribal resistance to NIGC efforts to clarify the distinction between Class II gaming, which does not require tribal-state compacts, and Class III gaming, which does, is another manifestation of this trend, and does not, in my

view, bode well for the continued success of the carefully crafted regulatory structure Congress established for Indian gaming.

The NIGC is currently a defendant in an action entitled Colorado River Indian Tribes vs. Hogen, pending in U.S. District Court for the District of Columbia, wherein the Colorado River Indian Tribes raise challenges to the application of the NIGC's Minimum Internal Control Standards to the Tribes' Class III gaming operations. The Tribes assert that while the NIGC may have a role with respect to Class II gaming activities, Class III gaming is governed solely by the tribal-state compact the Tribes negotiated with the State of Arizona.

If the Tribes prevail, and the holding is applied throughout the Indian gaming industry, the NIGC's oversight regulatory role would be severely curtailed. In my opinion, if this were to happen, a vacuum with respect to tribal gaming regulation would be reasonably perceived and cause the states, and perhaps Congress, to step in to fill the void and create a more onerous regulatory structure than presently exists. This I believe would be contrary to tribes' best interests.

The NIGC currently plays a vital and effective role with respect to oversight of all commercial tribal gaming - Class 11 and Class 111. The use and application of its Minimum Internal Control Standards is one of the primary tools utilized in carrying out this important federal oversight role. The Indian gaming industry and the NIGC will await and watch with interest developments in this litigation. Should the NIGC's Minimum Internal Control Standards be held inapplicable to Class III gaming, the NIGC will ask this Committee to consider and support legislation to restore and clarify that authority, as originally suggested in S 1529, which was introduced in the 108th Congress.

CHALLENGES TO NIGC'S REGULATORY ROLE

Among the difficult decisions the NIGC confronts daily is how to distinguish Class II games played with computer, electronic and other technologic aids, which do not require tribal-state com-

pacts, and Class III slot machines and electronic facsimiles of games of chance, which do require tribal-state compacts.

Dramatic strides have been made in technology with respect to gaming activities since the enactment of IGRA in 1988. Electronic player stations, linked to central computer servers, have been developed and utilized in the play of games Congress identified as Class 11, such as bingo and pulltabs.

These electronic player stations, and the servers to which they are attached, automate the play of bingo.The player stations display bingo cards electronically on video screens. The server draws numbers in batches or groups, and the player stations allow players to "daub" matching numbers on their cards all at once, with the press of a button or touch of the video screen.Often, the player stations add entertaining video displays. After the numbers are drawn and marked, and winning bingo patters are determined, the player stations display equivalent winning (and losing) results in the form of video slots machine reels, poker hands, or even horse races.Payment of bingo happens right at the player station, either electronically or in the form of a ticket or voucher.

The Johnson Act (15 U.S.C. SS 1171-1178) broadly defines and prohibits the use and possession of gambling devices in Indian country. IGRA provides that Johnson Act gambling devices may be used in Indian country under tribal-state compacts. IGRA further provides, however, that Class II games may be played with the use of computers, electronic, and other technologic aids. Thus, the question arises: does the Johnson Act prohibit the use and possession of a gambling device in Indian country, if the device is a permissible technologic aid to the operation and play of Class II gaming under IGRA?

Several courts that have addressed this question have disagreed with the position of the United States that the Johnson Act's prohibitions against the use and possession of gambling devices apply

to Class II. Nonetheless, there are limitations to what the courts that have addressed this issue have said about the extent of permissible Class II gaming. A myth has developed in this area that there are few limitations on the use of such equipment. In fact, the circuit court opinions that have been rendered are really relatively narrow, and, for the most part, confine themselves to the characteristics of the gaming machines presented in those cases. The United States government recently petitioned the United States Supreme Court to review two of these decisions, but the Supreme Court declined to undertake that review. Consequently, there has been difficulty in enforcing the Johnson Act, and, there has been less restraint on tribes or gaming equipment manufacturers from moving in the direction of Class II games that resemble slot machines more and more.

When the NIGC encounters gaming equipment that it perceives as going beyond electronic aids to the play of bingo, or pull-tabs being played without the benefit of a Class III compact, we ask tribes to discontinue such play or obtain the necessary tribal state compacts to authorize that play. There has been considerable voluntary compliance by tribes, but that has not been universal. Consequently, the NIGC has been forced to take enforcement action in a number of instances, several of which resulted in the closure of tribal gaming facilities and the imposition of fines on tribes amounting to millions of dollars.

The NIGC has also been asked, on a regular basis, to issue advisory opinions with respect to various electronic player stations and related equipment intended for use as technologic aids in the play of Class II games. In a number of instances, the NIGC has opined that such equipment, if played as represented, would constitute permissible Class II gaming aids. Other opinions have found the purported Class II aids to be Class III facsimiles or slot machines. These opinions were not final or official NIGC actions, but were merely advisory in nature. They have taken weeks,

months, and, in some cases, years to prepare, and, in many instances, were obsolete when issued, since the equipment to which they applied was no longer being used.

Hence, a great need currently exists to bring clarity to the distinction between Class II technologic aids and Class III electronic facsimiles and slot machines. This line has become blurred, by advances in technology. This lack of clarity, as well as different views on the applicability of the Johnson Act to legitimate Class II technologic aids, undermines the regulatory structure that Congress established for Class II and Class III Indian gaming in IGRA.

Recognizing the seriousness of the problem, the NIGC embarked upon an effort to clarify these issues by consulting with tribes and by assembling a joint federal-tribal advisory committee, which includes tribal gaming experts nominated by the gaming tribes. The NIGC attempted to be as transparent as possible in this effort, formulating drafts of proposed classification and technical standards, publishing those drafts on its website, and asking for, receiving and reviewing tribal comments on those drafts. The latest manifestation of this effort was the publication of the NIGC's fourth draft of proposed Class II electronic game classification standards on January 7, 2005, and the second draft of its proposed Class 11 game technical standards on February 2, 2005.

An action was initiated in U.S. District Court in the District of Columbia in March of 2005, seeking to enjoin this effort on the basis that the use of a tribal advisory committee violated the Federal Advisory Committee Act. The Confederated Salish and Kootenai Tribes and the Santa Rosa Rancheria sought a temporary restraining order, although that request was denied. Litigation continues, and the relief those tribes seek includes suspension of the NIGC's current rulemaking effort and a requirement that the NIGC start over again on the regulations. .

The NIGC submits that its draft regulations would bring clarity to the issue. The NIGC has carefully studied the legislative history of IGRA, as well as the court opinions that have addressed these

issues. The NIGC sincerely wants to draft regulations that will permit tribal use of computers and electronic technologic aids in the play of Class if games, yet not transgress the limits established by the IGRA. That is, the regulations should not be used as a pretext to permit the play of Class III electronic facsimiles of games of chance or slot machines without a tribal-state compact.

I firmly believe that Congress, in the passage of IGRA, intended that a difference was to exist between equipment used to aid the play of Class II games and gaming that requires tribal-state compacts. I further believe that Congress intended that this distinction be more than an arcane mathematical difference in the algorithm contained within a computer chip in an electronic player station or linked computer server for the play of bingo, and the algorithm in the computer chip that operates a slot machine. I believe that Congress understood that the bingo it described in IGRA was a competitive game actively played among participating players. I believe that it included language permitting the use of computer, electronic and other technologic aids to the play of Class 11 games to enhance that competitive participation, but also intended that these technologic aids were to be distinguished from computerized electronic gaming machines that automatically perform all, or nearly all, of the functions required in the game.

I am trying to implement and administer a set of regulations that will be consistent with the intent underlying IGRA. I believe that if tribes attempt to find a "loophole" in IGRA, where Class II gaming equipment so closely parallels Class III facsimiles and slot machines, then the carefully crafted regulatory structure of IGRA will disintegrate. In the end, the advantageous position that tribes have negotiated under the Class III compact structure, which has afforded them exclusivity with respects to gaming opportunities in some cases and market advantages in others, will be destroyed, as states move to permit non-Indian enterprises to expand and compete with tribes, and, perhaps, saturate gaming markets where tribes currently enjoy advantages. Such gaming prolifera-

tion would not further the stated purposes of IGRA nor inure to the benefit of tribes and tribal members who desperately need continued economic development opportunities. The NIGC soon will need to determine its course with respect to the regulations it has under consideration.

The NIGC stands very ready to receive any guidance this Committee might have to offer, and if the Committee perceives the NIGC's perceptions of the Class II/Class III structure intended in IGRA to be inapposite, the NIGC would greatly benefit from the Committee's view in this connection. This important issue remains one of the NIGC's principal challenges in the days ahead, and, if and when resolution comes to this matter, the industry will be well served.

As referenced above, the NIGC's Minimum Internal Control Standards continue to be one of the NIGC's most effective tools in strengthening regulation throughout Indian gaming and permitting the NIGC to adequately fulfill its oversight rule. Just as technological advances mandate constant vigilance in the area of game classification, technological advances mandate continuous review and modernization of the Minimum Internal Control Standards. To this end, the NIGC has formed a tribal advisory committee, has periodically reviewed its MICS, and has published in the Federal Register two sets of proposed changes to enhance those internal control standards. This will be an ongoing effort.

STRENGTHS AND WEAKNESSES IN IGRA'S STRUCTURE

The NIGC's inspectors and auditors, working from five regional offices, four satellite offices, and the NIGC headquarters in Washington, D.C., have maintained a continual oversight presence at tribal gaming facilities throughout the country. Most of what the NIGC's inspections and audits have observed and disclosed have been the positive operational and regulatory efforts of tribal governments, acting both independently, and in the case of Class III gaming, together with state participation to ensure adequate regulation of tribal gaming enterprises. In many instances, however, regu-

latory weaknesses, and instances of risk and loss to tribal gaming revenues, assets and the integrity of tribal gaming, have been identified. While many tribes have developed and implemented sophisticated and effective regulatory structures and controls, and invested large sums of money and other resources for regulation of their gaming operations, many others have not.

On one hand, as the result of our oversight efforts, the NIGC can report to the Committee numerous examples of tribes doing an outstanding job of ensuring the integrity of their gaming operations. Under their authority as primary regulators, tribes regularly deny licenses to unsuitable employees and to unsuitable vendors who have sold illegal machines or engaged in questionable business practices; remove individuals managing their gaming operations without NIGC approved management contracts; detect and report suspected criminal activities to the appropriate law enforcement agencies; and develop and implement internal controls that equal, and often surpass, those in place in non-Indian casinos. The overwhelming, majority of tribes also do an excellent job of ensuring that the gaming revenues from their operations are used for the purposes authorized under IGRA.

On the other hand, NIGC oversight regularly uncovers serious breakdowns in regulation at Class II and Class III tribal gaming operations throughout the country, even where apparent adequate tribal regulation and control is in place. Examples of instances where tribal gaming operational and regulatory efforts have been found deficient include the following:

During the course of investigations and Minimum Internal Control compliance audits, NIGC investigators and auditors discovered that an extraordinary amount of money was flowing through two off- track betting (OTB) operations on two reservations. The amount of money was so high in comparison to the amount that could reasonably flow through such OTB operations that our investigators immediately suspected money laundering or similar activities. These two operations were the

first referrals to the FBI's working group in which we participate. The FBI investigations found that they were part of a widespread network of such operations off reservation as well, with organized crime links and several federal criminal law violations. Unfortunately, the tribes' gaming management allowed them to gain access and operate as part of their Class III tribal gaming operations, and the tribes' gaming regulators completely failed to take any action against these illegal OTB operations.

There are also examples where tribes continued to operate, without modification or correction, a gaming facility that had long been identified as a serious fire hazard; permitted gaming activities to be conducted by companies owned by individuals with known criminal associations; distributed large amounts of gaming revenues without requisite approved revenue allocation plans or the financial controls necessary to account for them; knowingly operated gaming machines that were plainly illegal; and appointed gaming commissioners and regulatory employees, and licensed and employed gaming employees whose criminal histories indicated that they were unsuitable and serious risks to the tribes' gaming enterprise. An accurate assessment of Indian gaming regulation must also reflect the unfortunate examples of tribes that are so politically divided that they are unable to adequately regulate their gaming activities, as well as instances where tribal officials have personally benefited from gaming revenues at the expense of the tribe itself. In addition, there have been many instances where apparent conflicts of interest have undermined the integrity and effectiveness of tribal gaming regulation. In all of these troubling situations, it was necessary for the NIGC to step in to address the problems.

The NIGC continues to address a number of Indian land questions. To approve a management contract, to approve site-specific tribal ordinances and to exercise our authority over Indian gaming, we must first decide whether the lands are Indian lands on which the tribe may conduct gaming.

Many gaming operations do not present any real issue. Those are generally tribal operations conducted on lands within the tribes' reservations, trust lands acquired prior to October of 1988, or trust lands in Oklahoma within the tribes' former reservations. Other Indian land questions can be far more complex and require ethnohistoncal research and extensive legal analysis. These complex questions are where we focus our resources. We do so by coordinating with the Department of the Interior, which also has an interest in our conclusions.

Finally, as the Committee reviews these issues, we encourage you to consider the proposed technical amendments to IGRA that were submitted to the President of the Senate on March 23, 2005. Those proposed amendments would standardize the NIGC's background investigation responsibilities so that Class III management contractors receive the same level of scrutiny that the NIGC exercises over Class II contractors; clarify the NIGC's authority; authorize the NIGC to pursue actions against individuals; require that tribal gaming commissioners and commission employees be subject to background investigations; and allow the NIGC's fee cap to fluctuate with expansion or contraction in the size of the industry.

We appreciate the time and attention that the Chairman and Committee are devoting to Indian gaming. If we can be of any assistance or answer any questions, do not hesitate to ask.

LOAD-DATE: April 27, 2005