American Indian Law Review

Volume 7 | Number 2

1-1-1979

Taxation: State Transaction Privilege Tax: An Interference with Tribal Self-Government

Sharon E. Claasen

TAXATION: STATE TRANSACTION PRIVILEGE TAX: AN INTERFERENCE WITH TRIBAL SELF-GOVERNMENT

Sharon E. Claassen

On the surface, the basic theory involving state taxation of Indians and Indian property appears relatively simple. Indians and Indian property could not be taxed by the state unless the state had been given the express power to do so. Only Congress could grant such power to the state. Indian property outside of the reservation, however, was subject to the state taxing power unless Congress had provided some form of applicable exemption.[1] The problems with this theory are twofold, *i.e.,* determining the intent of congressional action or inaction in the area and defining what activities or enterprises are on the reservation or off the reservation. As the tribes moved from an isolated reservation existence and became involved in exchanges with surrounding state communities, a large area of uncertainty evolved. Increased interaction between tribes and state citizens raised taxation issues that had not been specifically addressed by Congress.

Given the lack of direct congressional guidance, the courts were left to create their own doctrines upon which to decide state taxation issues.[2] Courts historically trudged through the cases overcoming or circumventing each obstacle as it arose. What has developed, therefore, is a hodgepodge of law that offers little guidance for either the state or the tribe.[3]

One of the more notable doctrines that developed in the area was the doctrine of "federal instrumentality." This concept actually originated in the case of *M'Culloch v. Maryland* in 1819.[4] The doctrine determined that certain activities were exempt from state taxation because they were important in furthering the objectives of the federal government. Private parties could claim

1. F. COHEN, FEDERAL INDIAN LAW 254 (1942).

2. Mescalero Apache Tribe v. O'Cheskey, 439 F. Supp. 1063, 1073 (D.N.M. 1977). "The whole area of state jurisdiction over non-Indians doing business with Indians on Indian lands deserves Congressional review and the enactment of definitive federal legislation. In their absence, the courts can only cope with each fact situation that arises within a framework of fragmentary legislation. Further the scope of the problem is such that it does not lend itself to resolution by the process of piece-meal adjudication. Yet this is precisely what must happen in the absence of Congressional action." *Id.* at 1074.

3. Barsh, *Issues in Federal, State and Tribal Taxation of Reservation Wealth: A Survey and Economic Critique,* 54 WASH. L. REV. 531, 533 (1979) [hereinafter cited as Barsh].

4. 17 U.S. (4 Wheat) 316 (1819).

this exemption upon proof that their function qualified as a "federal instrumentality."[5] This doctrine was transposed to Indian law in 1903 in the case of *United States v. Richert*[6]:

> The doctrine in its application to Indians and Indian property is founded upon the premise that the power and duty of governing and protecting tribal Indians is primarily a federal function and that a state cannot impose a tax which will substantially impede or burden the functioning of the Federal Government.[7]

One of the primary uses of this doctrine was to foreclose any state taxation of non-Indian leaseholders of Indian lands.[8] As the development of Indian lands increased, especially in mineral and oil and gas exploitation, this exemption came under close scrutiny by the courts. The states argued that non-Indian leaseholders were wrongfully avoiding valid state taxation and thus the non-Indian leaseholders and not the Indians were benefited. The courts agreed and in 1949 they rejected the federal instrumentality exemption from state taxes as it applied to non-Indian lessees.[9] The federal instrumentality doctrine continued to lose its influence until, for all practical purposes, it was pronounced dead.[10]

The demise of the instrumentality doctrine opened the door for state taxation encroachment on Indian tribes. A new wave of cases appeared that exposed the vehicle of this encroachment—the tax on gross receipts, usually in the form of a transaction privilege tax.[11] The tax in question is levied on the privilege of engaging in certain activities within the state. It usually includes the performance of services, including construction.[12] The tax is not levied on the sale or service, but it is measured by the gross receipts of the sale or service.[13] The obligation created by the

5. Note, *The Ninth Circuit's Federal instrumentality Doctrine—A Threat to Tribal Sovereignty*, 53 NOTRE DAME LAW. 358, 359 (1942).

6. 188 U.S. 432 (1903).

7. F. COHEN, FEDERAL INDIAN LAW 254, 255 (1942).

8. Choctaw & Gulf R.R. v. Harrison, 235 U.S. 292 (1914).

9. Oklahoma Tax Comm'n v. Texas, 336 U.S. 342 (1949).

10. Mescalero Apache Tribe v. Jones, 411 U.S. 145 (1973).

11. ARIZ. REV. STAT. §§ 42-1301 to 42-1362 (Supp. 1979); N.M. STAT. ANN. § 72-16A (Supp. 1975). These two statutes are examples of this tax. Most of the litigation discussed herein involved one of these two jurisdictions.

12. ARIZ. REV. STAT. § 42-1310(i) (Supp. 1979).

13. Arizona Tax Comm'n v. Southwest Kenworth, Inc., 561 P.2d 575 (Ariz. 1977).

transaction privilege tax is incurred only by the person or corporation doing business in the state.[14]

The implementation of this tax has created a figurative mine field for Indian tribes and those engaging in business with the tribes. This note will trace the development of case law in the area. The study is centered on the application of the transaction privilege tax to non-Indian contractors doing business on Indian lands. The resulting effects upon the development of the Indian tribes will be considered. Finally, the note will discuss tribal actions that potentially could offset the effects of the transaction privilege tax.

Non-Indians Doing Business With Indians

The problem in the area of state tax litigation where non-Indians engaged in business with Indians was summarized by Judge Bratton in the case of *Mescalero Apache Tribe v. O'Cheskey.*[15]

> This case has presented one aspect of a problem that is with increasing frequency facing the courts. On one side are the Indians, subject to the plenary power of Congress. On the other side are the states, anxious to control what transpires within their borders and to raise revenues from whatever source they can. There is currently strong Indian resistance to any state effort to exert control over or to tax non-Indians doing business with Indians. There is an equally strong effort by the states to fill with state laws any void existing by virtue of Congress's failure to enact governing legislation. Between them stand the courts, hampered by Congressional inaction on the subject.[16]

One of the earlier cases involving the application of a state transaction privilege tax (sometimes referred to as an excise tax)[17] to a non-Indian doing business with Indians was *Warren Trading Post Co. v. Arizona Tax Commission.*[18] The state of Arizona had

14. ARIZ. REV. STAT. § 42-1309 (Supp. 1979), as interpreted by New Cornelia Co-op Mercantile Co. v. Arizona Tax Comm'n, 533 P.2d 84 (Ariz. 1975).

15. 439 F. Supp. 1063 (D.N.M. 1977).

16. *Id.* at 1074.

17. It is important to remember that for the purposes of this paper, "excise" tax will refer only to the transaction privilege tax. The term "excise tax" has been held to be synonymous with "privilege" or "license" tax. *See* American Airways v. Wallace, 57 F.2d 877, 880 (D. Tenn. 1932).

18. 380 U.S. 685 (1965).

levied an excise tax on the "gross proceeds of sales or gross income" of the trader.[19] The trader had been granted a license to operate a retail business on the Navajo Indian Reservation. The United States Commissioner of Indian Affairs had issued the license pursuant to Section 261 of Title 25 of the United States Code (1958). The Court held that the federal regulation of Indian traders was so comprehensive that the federal government had in fact preempted the area. Therefore, the Arizona excise tax could not be applied to Indian traders.[20]

In *Warren Trading Post* the Court noted that if this state excise tax was allowed to stand, it would place economic burdens on the traders or the Indians. The excise tax would be in addition to any taxes either the tribes or Congress imposed in this area. The Court concluded that a state tax could increase prices and this was not in accord with the congressional plan to "protect Indians against prices deemed unfair or unreasonable."[21] This benevolent language did not include any mention of the "infringement test" established in *Williams v. Lee.*[22] The Court did allude to the unacceptability of federal, state, and tribal regulations all imposing economic burdens in this area. However, the Court avoided any discussion of state infringement on the tribal government. If the Court was equating economic burden with the tribe's ability to govern itself, then possibly an infringement argument could be made against the tax. Given the glancing treatment by the Court and the inclusion of protective intent, however, such an argument would be tenuous at best.

In 1975, *Matheson v. Kinnear,* a cigarette tax case, was decided.[23] The case, though addressing the validity of a sales tax, raised a relevant question. The petitioner argued that his land, upon which the business was located, was exempt from taxation and therefore his business was also exempt. Petitioner, whose land was exempted from state taxation,[24] further argued that the language of Section 412(1) specifically designated such lands as

19. ARIZ. REV. STAT. §§ 42-1309, 42-1312 (1956). Both sections have since been amended, ARIZ. REV. STAT. §§ 42-1309, 42-1312 (Supp. 1979).

20. Warren Trading Post Co. v. Arizona Tax Comm'n, 380 U.S. 685, 691 (1965).

21. *Id.*

22. Williams v. Lee, 358 U.S. 217, 220 (1959): "Essentially, absent governing Acts of Congress, the question has always been whether the state action infringed on the right of reservation Indians to make their own laws and be ruled by them."

23. 383 F. Supp. 1025 (W.D. Wash. 1975).

24. 25 U.S.C. § 412(a) (1970). This section also provides an exception for certain lands which are classified as Indian homestead lands. 25 U.S.C. § 412(d) (1970).

"federal instrumentalities." He noted that in *Mescalero Apache Tribe v. Jones,* the Court had held that 25 U.S.C. § 465[25] did not exempt the activity carried out on the land even though the land itself was exempt. Section 465 did not designate the exempt lands as federal instrumentalities. Therefore, he concluded that the land involved in *Mescalero* was not a federal instrumentality and thus neither was the activity carried thereon. Conversely, as 25 U.S.C. § 412(a) did designate the land as a federal instrumentality, the activity thereon was also so classified and thus exempt from state tax.

The Court disagreed, holding that land covered under both Section 412(a) and Section 465 qualified as federal instrumentalities. However, the Court emphasized that the decision rested on the fact that the phrase "federal instrumentality" pertained only to the land and not to the business activities conducted on the land.[26] The Court also reiterated the general rule that tax exemptions cannot be granted by implication.[27] Therefore, cigarette sales on petitioner's lands were not exempt from state taxation.[28]

This innovative argument illustrated the fact that merely because the courts denounce a once established legal theory, this does not prevent the reappearance of the theory in a slightly different context.[29] *Matheson v. Kinnear* firmly established the rule that the court would not find a tax exemption solely because the activity in question occurred on tax-exempt land.[30] The activity itself must qualify for the exemption. This was to develop into a significant obstacle in the cases involving non-Indian contractors working on Indian land.

In 1976 the first of a series of non-Indian contractor suits reached the courts. *G. M. Shupe, Inc. v. Bureau of Revenue,* involved a non-Indian Washington contractor who was employed to construct the Nambe Pueblo Dam on the Nambe Pueblo Reservation.[31] The plaintiff in this case appealed the imposition

25. The section discussed in Mescalero Apache Tribe v. Jones, 411 U.S. 145 (1973), provides that: "any lands or rights acquired pursuant to [the 1934 Act] shall be taken in the name of the United States in trust for the Indian tribe . . . for which the land is acquired, and such lands or rights shall be exempt from State and local taxation." 25 U.S.C. § 465 (1970).

26. Matheson v. Kinnear, 393 F. Supp. 1025, 1032 (W.D. Wash. 1975).

27. *Id.* at 1033. *See* Mescalero Apache Tribe v. Jones, 411 U.S. 145, 156 (1973); Oklahoma Tax Comm'n v. Texas Co., 336 U.S. 342, 365-66 (1949).

28. Matheson v. Kinnear, 393 F. Supp. 1025, 1033 (W.D. Wash. 1975).

29. See text accompanying note 10, *supra.*

30. Matheson v. Kinnear, 393 F. Supp. 1024 (W.D. Wash. 1975).

31. 550 P.2d 277 (N.M. Ct. App. 1976).

of the New Mexico gross receipts tax.[32] The court dismissed the argument that New Mexico lacked the jurisdiction to impose this tax. The court noted numerous decisions that had held that "activities by non-Indians on Indian land have generally been held not exempt from state taxation."[33]

There were, however, two issues that were determinative as to the validity of the state excise tax. The first issue involved the federal preemption doctrine established in *Warren Trading Post Co. v. Arizona Tax Commission*.[34] The court found that the substantial federal regulation present in *Warren Trading Post* was absent in this case. The plaintiff offered the alternative argument that even if comprehensive federal regulations did not exist, the state excise tax on the holder of a federal contract frustrated federal Indian policies. This the court viewed as a "federal instrumentality" argument. In essence the contractor was alleging that the performance of the contract was in furtherance of a federal policy to develop Indian lands. This argument, the court held, "has been rejected in numerous federal instrumentality cases."[35]

The second issue the court explored involved the possible infringement on the Indians' rights of self-government. The court turned to the test of *Williams v. Lee*,[36] noting that this test applied in conflicts between state and tribal interests.[37] The court found no infringement. The Nambe Indians had not employed the contractor nor were they paying him. The contractor had been employed by the United States Department of the Interior, Bureau of Reclamation.[38] Furthermore, the court noted that the Nambe Indians had not asserted tax jurisdiction over the activity in question. Under these circumstances, no direct financial

32. *Id.* at 278.

33. *Id.* at 279.

34. 380 U.S. 685, 691 (1965). See also text accompanying note 20, *supra.*

35. G.M. Shupe, Inc. v. Bureau of Revenue, 550 P.2d 277, 279-80 (N.M. Ct. App. 1976).

36. 358 U.S. 217, 220 (1959). See note 22, *supra.*

37. G.M. Shupe, Inc. v. Bureau of Revenue, 550 P.2d 277, 279-80 (N.M. Ct. App. 1976), *citing* McClanahan v. Arizona Tax Comm'n, 411 U.S. 164, 179 (1973): "It must be remembered that cases applying the Williams test have dealt principally with situations involving non-Indians. . . . In these situations, both the tribe and the State could fairly claim an interest in asserting their respective jurisdictions. The Williams test was designed to resolve this conflict by providing that the State could protect its interest up to the point where tribal self-government would be affected."

38. G.M. Shupe, Inc. v. Bureau of Revenue, 550 P.2d 277, 282 (N.M. Ct. App. 1976).

burden would be sustained by the Nambe Indians and the tax was held valid.

Department of Revenue v. Hane Construction Co. also involved an out-of-state non-Indian contractor.[39] The state of Arizona had imposed its excise tax on the gross receipts the contractor received from work on canals located on the Colorado River Indian Reservation. Hane had come to the state solely for the purpose of fulfilling this contract with the Bureau of Indian Affairs. The court held that although there were significant federal regulations that applied to this type of contract, these regulations had specifically recognized the possibility of an applicable state tax.[40] In determining the issue of infringement, the court noted that the contractor could not legally pass the tax on to the tribe. Even if this had occurred, in this case the project was funded by public, not tribal, monies. The only possible result could be that there would be fewer BIA funds available to the tribe and the court found this to be too remote to establish infringement.[41]

A possible solution to the problem involved in the developing line of cases is suggested by *Mescalero Apache Tribe v. O'Cheskey.*[42] This case can be divided into two decisions: the first may provide a method for future use, the second points out the problems still to be overcome. The state of New Mexico had imposed its excise tax on certain non-Indian contractors working on projects on the Mescalero reservation. The tribe had entered into an indemnity agreement with all the contractors which provided for reimbursement if such an excise tax should be assessed.[43]

The first part of the case to be considered involved Quiller Construction Company. Quiller was employed to build 100 houses. This employment involved a complex series of contracts and agreements that included the tribe, the Mescalero Apache Tribe Housing Authority (an agency of the tribe), OGO (a California firm that planned the project and arranged financing), and Quiller.[44] The court examined the various documents and held that Quiller was in fact an agent of the tribe. This agency, the court continued, exempted Quiller from the state excise tax imposed on the purchase of materials. This was based on the

39. 564 P.2d 932 (Ariz. 1977).
40. *Id.* at 934.
41. *Id.*
42. 439 F. Supp. 1063 (D.N.M. 1977).
43. *Id.* at 1066.
44. *Id.* at 1069-70.

evidence that all materials ordered by Quiller were billed to the tribe. It was irrelevant that Quiller had been made the tribe's agent to avoid the excise tax. The tax exemption was not held to include monies received by Quiller for its services rendered on the housing project.[45]

While the agency theory appears to be a method by which tribes can avoid the imposition of state excise taxes on their contracts with non-Indians, it has a major limitation. The tax did not apply to the materials purchased by Quiller as the tribe's agent because the New Mexico statute exempts sales of tangible personal property to an Indian tribe.[46] This exemption was the basis for the court's avoidance of the excise tax as to the materials.[47]

The second part of this decision involved the application of the excise tax to the services rendered by non-Indian contractors. In deciding this issue, the court noted that while the legal incidence of the tax is upon the contractors only, it will in reality be passed to the purchaser. This was inevitable in this case because the tribe had entered into agreements to reimburse the contractors should the tax be imposed. Despite this, the court held this to be nothing more than an indirect burden on the tribe.[48]

At the time the services in question were performed, the tribe had enacted its own gross receipts tax and licensing ordinances. It should be noted that in *G. M. Shupe,*[49] the court had considered the absence of such tribal legislation when it determined that the excise tax did not constitute infringement on tribal self-government.[50] Faced with the existence of an identical tribal tax, the court held that there was no infringement. The justification for this ruling apparently involved the benefits by and protection from the state that had been utilized by the contractors as they travelled to and from the reservation.[51]

The court continued to reject the preemption arguments of the tribe. The fact that the tribe was organized under the Indian Reorganization Act[52] did not support the preemption theory. The

45. *Id.* at 1071.

46. N.M. STAT. ANN. § 72-16A-14.9 (Supp. 1975).

47. Mescalero Apache Tribe v. O'Cheskey, 439 F. Supp. 1063, 1070-71 (D.N.M. 1977).

48. *Id.* at 1072.

49. G.M. Shupe, Inc. v. Bureau of Revenue, 550 P.2d 277, 280 (N.M. Ct. App. 1976).

50. See text accompanying note 38, *supra.*

51. Mescalero Apache Tribe v. O'Cheskey, 439 F. Supp. 1063, 1073 (D.N.M. 1977).

52. 25 U.S.C. § 461 (1970).

court acknowledged that the purpose of this Act was to encourage tribal development but held that this development was not affected where only an economic burden falls on the tribe. The legal incidence of the tax, ruled the court, does not fall on the tribe, therefore no preemption.[53]

In 1978 two Arizona cases were decided that considered the state's excise tax. *White Mountain Apache Tribe v. Bracker* involved a non-Indian carrier that had contracted with the tribe to sell, load, and transport lumber on the reservation.[54] The state had imposed an excise tax on the carrier's services, which, with few exemptions, were carried out only on roads built by the BIA, the tribe, or the carrier itself.[55] Despite the fact the carrier's activities were totally upon the reservation under direct contract with the tribe, the court held that the tax applied because the reservation was contained within the state boundaries.[56] The fact that the tribe would ultimately pay the $9,000 annual tax did not constitute infringement.[57] Merely because the economic burden will ultimately fall on a "non-tax-paying entity," the court stated, will not invalidate the state tax.[58] Indeed, because the tribe had agreed to pay the excise tax if imposed, it had placed itself in the position of a "mere volunteer" and therefore could not complain.[59]

The second Arizona case, *Arizona Tax Commission v. Central Machinery Co.*,[60] was decided by the Arizona Supreme Court sitting en banc. The court held that the state excise tax applied to the plaintiff, reversing the district court ruling. Plaintiff was a non-Indian farm equipment seller. The activity in question involved a sale of eleven tractors to Gila River Farms, an enterprise of the Gila River Indian Community.[61] The tax amounted to $2,916.62 and was included in the total sales price of $100,137.26. Although the plaintiff had not obtained a federal license, the

53. Mescalero Apache Tribe v. O'Cheskey, 439 F. Supp. 1063, 1073 (D.N.M. 1977).
54. 585 P.2d 891, 894 (Ariz. 1978).
55. *Id.*
56. *Id.* at 896.
57. *Id.* at 899.
58. *Id.* at 897.
59. *Id.*
60. 589 P.2d 426 (Ariz. 1978).
61. "The Gila River Indian Community is an Indian Entity existing under the authority of 48 Stat. 984, 25 U.S.C. §§ 461 et seq." *Id.*

superintendent of the agency could have excluded it from conducting business on the reservation.[62]

The court rejected plaintiff's argument that it was an Indian trader within the meaning of *Warren Trading Post.*[63] There was no federal preemption and the tax applied. This, the court noted, was sufficient to uphold the tax. The court felt compelled to reject the "ultimate burden" argument, however, and reiterated that merely because the Indians would sustain the economic burden, this did not make the plaintiff immune from the state tax.[64]

Both of the above discussed Arizona decisions have been appealed to the United States Supreme Court.[65] It will be the first time the Supreme Court has addressed the question of the application of a state transaction privilege tax to non-Indians doing business with Indians since *Warren Trading Post* was decided in 1965. The cases are being considered together.[66] It will be interesting to see whether the fact that *White Mountain Apache Tribe v. Bracker*[67] was filed by the tribe itself will affect the Court's decision. It is unfortunate that neither of the tribes involved appear to have implemented tribal legislation in this area. The key issues raised by the cases appear to be: (1) What is an Indian trader within the meaning of *Warren Trading Post*?[68] (2) If the "ultimate burden" of the tax falls upon the tribe, can the tax be held not to infringe on tribal self-government?

The Effect on the Tribes

It becomes apparent from a reading of the cases that a strong presumption exists in favor of the state's ability to tax anyone engaging in business within that state's boundaries. Judge Sutin, especially concurring in *G. M. Shupe, Inc. v. Bureau of Revenue,*[69] stated that: "Where the activity of the Indians obstructs the operation of state laws and is inconsistent with the political welfare of the state and the social advantage of its

62. *Id.* at 427.
63. Warrent Trading Post Co. v. Arizona Tax Comm'n, 380 U.S. 685 (1965).
64. State v. Central Machinery Co., 589 P.2d 426, 427 (Ariz. 1978).
65. 100 S.Ct. 41 (1979) (oral arguments set).
66. *Id.*
67. 585 P.2d 891 (Ariz. 1978).
68. Warren Trading Post Co. v. Arizona Tax Comm'n, 380 U.S. 685 (1965).
69. 550 P.2d 277 (N.M. Ct. App. 1976).

citizens, Indian 'inherent sovereignty' must give way to the power of the state to enact legislation."[70]

This is strong language, but it reflects the attitude of the state courts. The question as to the states' power to tax non-Indians living on the reservation has been settled.[71] These cases provide more of a basis for allowing state control. However, when the state is asserting control over an out-of-state, non-Indian contractor who comes into the state for the sole purpose of fulfilling a contract with a tribe and whose business is conducted entirely within the reservation, the basis lacks sufficient justification. An excellent example is presented in *Tiffany Construction Co. v. Bureau of Revenue.*[72] Tiffany was a non-Indian Arizona corporation. The corporation contracted with the Navajo Tribe to grade and drain a road on the portion of the Navajo Reservation that fell within the boundaries of New Mexico. All work was performed on the reservation and all the employees were either Arizona residents or Navajo Reservation Indians, who always entered and exited the reservation on the Arizona side. New Mexico claimed that Tiffany owed the state $78,583.03 as a transaction privilege tax on the project, which totaled approximately $1,681,740.[73] The contact that Tiffany had with New Mexico was found as follows: "Tiffany enjoyed the use of roads located on the reservation but maintained by the State, and that it benefited from the New Mexico Environmental Improvement Agency's regulation of air pollution from the Four Corners Power Plant.[74]

Several cases have discussed the fourteenth amendment due process argument.[75] For a state tax to apply to an out-of-state corporation, there must be a minimal contact with the state.[76] The *Tiffany* case illustrates just how minimal this contact can be.[77] The questionable area develops when there are no real benefits or contacts with the state except to work on a reserva-

70. *Id.* at 282.

71. Surplus Trading Co. v. Cook, 281 U.S. 647 (1930); Thomas v. Gay, 169 U.S. 264 (1898); Utah & Northern R.R. v. Fisher, 116 U.S. 28 (1885).

72. 603 P.2d 332 (N.M. Ct. App. 1979).

73. *Id.* at 333.

74. *Id.* at 334.

75. Mescalero Apache Tribe v. O'Cheskey, 439 F. Supp. 1063, 1074 (D.N.M. 1977); Department of Revenue v. Hane Constr. Co., 564 P.2d 932, 935 (Ariz. 1977); G.M. Shupe, Inc. v. Bureau of Revenue, 550 P.2d 277 (N.M. Ct. App. 1976).

76. Department of Revenue v. Hane Constr. Co., 564 P.2d 932, 934-35 (Ariz. 1977).

77. Tiffany Constr. Co. v. Bureau of Revenue, 603 P.2d 332 (N.M. Ct. App. 1979).

tion. Driving through the state to reach the reservation may not be sufficient in light of an apparent trend by the Supreme Court to redefine minimal contact.[78] The state's interest in controlling the transaction of business within its borders appears to allow the courts to ignore the jurisdictional status of the reservation.[79] The states should not be allowed to continue to treat a reservation as one of its own counties. This attitude presents a substantial threat to tribal sovereignty and it must be arrested.

The application of the state transaction privilege tax also affects the economic position of the tribe. The tribes are placed in a situation where they must enter into an actual agreement to pay this tax[80] or the cost is included in the contract price paid by the tribe.[81] The cases consistently hold that the contractors should not be allowed to escape payment of the tax simply because they contract with Indians.[82] Regardless of where the legal incidence of the tax falls, the courts have also admitted that it is the tribes who will pay the tax.[83] In effect, the courts have constructed a legal fiction which in reality allows the state to collect the tax from the tribe. Therefore, it is the tribe which is prevented from utilizing its tax exempt status and the contractor is merely incidental.[84]

Another effect of the state excise tax allowance is to create a double taxation for the contractor where the tribe has initiated its own taxing and licensing system. The courts have found that this situation does not result in an interference with tribal self-government.[85] In *Confederated Tribes of the Colville Indian Reservation v. Washington,*[86] the federal district court held that Washington's cigarette excise tax could not be applied to Indian vendors' reservation sales to non-Indians.[87] The court found the enactment of tribal tax ordinances had preempted the state tax.

78. *See* World-Wide Volkswagen Corp. v. Woodson, 100 S.Ct. 559 (1980).

79. Department of Revenue v. Hane Constr. Co., 564 P.2d 932, 934-35 (Ariz. 1977).

80. Mescalero Apache Tribe v. O'Cheskey, 438 F. Supp. 1063, 1066 (D.N.M. 1977).

81. State v. Central Machinery Co., 589 P.2d 426 (Ariz. 1978).

82. Mescalero Apache Tribe v. O'Cheskey, 439 F. Supp. 1063, 1072 (D.N.M. 1977); "The umbrella of immunity from state taxation covering reservation land and income earned on the reservation by a reservation Indian is not wide enough to shield non-Indian contractors of its imposition."

83. *Id.* at 1072.

84. This effect can be compared to the problems with the actual economic burden in the cigarette tax cases. *See* Barsh, *supra* note 3.

85. Mescalero Apache Tribe v. O'Cheskey, 439 F. Supp. 1063, 1073 (D.N.M. 1977).

86. 446 F. Supp. 1339 (E.D. Wash. 1978).

87. *Id.* at 1362.

Under these circumstances, the imposition of the state tax did constitute an interference with tribal self-government. The interference must, however, be based upon a showing that the state tax would lead to a substantial reduction of tribal tax revenues.[88] However, on June 10, 1980, the United States Supreme Court reversed this district court ruling.[89] The Court held that the tribe could not preempt an otherwise valid state cigarette sales tax by enacting their own similar tax.[90] It appears that the Court was preoccupied by the fact that the only tribal product involved was the tax exemption itself. The Court noted that, "although taxes can be used for distributive or regulatory purposes, as well as for raising revenue, we see no nonrevenue purposes to the tribal taxes at issue. . . ."[91] This language allows speculation that should the transaction privilege tax be classified as a regulatory tax, the *Colville* rationale might not apply.

Tribal Actions

If the tribes could establish a regulatory tax on non-Indian contractors working on the reservation, the argument of tribal preemption might be feasible. The tribes would have to implement their own transaction privilege tax. Furthermore, it would be essential to enact corresponding licensing provisions. This would help to foreclose the state's argument that the state must regulate all transactions within state boundaries. While these measures could possibly eliminate the problems associated with a solely revenue-generating tax, there would be other difficult issues.

The question of state control over foreign corporations would have to be addressed. Adoption of licensing legislation by a tribe might weaken the argument. However, a construction project is somewhat more complex than the sale of cigarettes. Therefore, there will be additional reasons for the state to argue that it has a legitimate interest above and beyond the tribal legislation.

If, however, these obstacles were overcome, not all tribes would be able to support the economic burden of such a taxation system. An alternative would be the use of a tribal-state revenue

88. *Id.* at 1360-63. *See* Barsh, *supra* note 3, at 570-72.

89. Washington v. Confederated Tribes of the Colville Reservation, 48 U.S.L.W. 4668 (U.S. June 10, 1980).

90. *Id.* at 4674.

91. *Id.*

compact. Under this arrangement the state would collect the tax and then remit a certain percentage to the tribe. The less attractive side of this type of arrangement is that the tribe becomes locked into the state tax system and thus loses flexibility, and more important, control over the tax.[92]

The establishment of a tribal taxation system is not a panacea. It could be discovered that the state tax remained applicable. A tribe would find contractors unimpressed by the prospect of paying two transaction privilege taxes. Other methods would than need to be employed. A tribe could use the agency theory applied in *Mescalero Apache Tribe v. O'Cheskey.*[93] It would be necessary in this instance that the same type of exemption be available. This alternative does not appear to offer widespread relief.

Tribes that possess sufficient economic resources should evaluate their future developmental priorities. It may be possible for the tribes to establish their own corporations. Not only would this allow an avoidance of the state tax, but it could provide employment and training for tribal members. An example is found in *Eastern Navajo Indus., Inc. v. Bureau of Revenue.*[94] In this case, the Navajos incorporated under the State Business Corporation Act.[95] The corporation produced and sold modular and prefabricated homes that were designated for purchase and occupancy by tribal members. The state's tax on gross receipts was held not to be applicable to this Indian corporation.[96]

Conclusion

This area of Indian law is basically unsettled at present. There are several cases awaiting decision by the United States Supreme Court. Until certain questions are addressed, the tribes remain in a dubious position. Even with possible answers forthcoming, the area will remain subject to the relentless efforts of the states seeking control over reservation projects and monies. Without specific congressional legislation, the issues will continue to be decided both slowly and narrowly. The courts have failed to acknowledge the seriousness of the state intrusion through this taxation. Until such recognition is reflected in court decisions, the

92. Barsh, *supra* note 3, at 575, 576.

93. 439 F. Supp. 1063, 1069-70 (D.N.M. 1977).

94. 552 P.2d 805 (N.M. Ct. App. 1976).

95. N.M. STAT. ANN. §§ 51(24)(1) to (31)(11) (1975).

96. Eastern Navajo Indus., Inc. v. Bureau of Revenue, 552 P.2d 805, 810 (N.M. Ct. App. 1976).

tribes will continue to lose control over their financial assets and their future development.

Editor's Note: Subsequent to acceptance of this note, the United States Supreme Court decided *Washington v. Confederated Tribes of the Colville Indian Reservation,* 100 S. Ct. 2069 (1980). This highly significant case arguably resolves the long-standing conflict regarding which entity—the state or the tribe—has legal authority to tax nontribal members residing or doing business on Indian reservations. For further information concerning *Colville,* see *Recent Developments*, this issue.