States' political relationship with Indian tribes. Tribes have a sovereign interest in achieving and maintaining economic self-sufficiency, and the federal government has an established policy of encouraging tribal self-governance and tribal economic self-sufficiency. A tribe-specific preference in accord with tribal law ensures that the economic development of a tribe's land inures to the tribe and its members. Tribal sovereign authority, which carries with it the right to exclude non-members, allows the tribe to regulate economic relationships on its reservation between itself and non-members. See, generally, *Equal Employment Opportunity Commission v. Peabody Western Coal Company,* No. 2:01-cv-01050 JWS (D. Ariz., Oct. 18, 2012) (upholding tribal preferences in leases of coal held in trust for the Navajo Nation and Hopi Tribe, but also citing with approval the use of such preferences in business leases). These regulations implement the established policy of encouraging tribal self-governance and tribal economic self-sufficiency by explicitly allowing for tribal employment preferences.

162.016 (PR 162.014) – BIA Compliance with Tribal Laws

- Restrict when BIA will defer to tribal law by changing "making decisions regarding leases" to "making the decision to approve or disapprove the proposed lease." We did not incorporate this change because BIA will defer to tribal law in decisions regarding leases beyond just the approval decision.

162.017 (PR N/A) – What Taxes Apply (New Section)

All tribal commenters supported proposed provisions clarifying that improvements on trust or restricted land are not taxable by non-tribal entities; however, many tribes requested clarification regarding other taxation arising in the context of leasing Indian land. For this reason, we separated this topic into its own section and

moved it from the residential, business, and WSR leasing subparts to subpart A. This section now addresses not only taxation of improvements on leased Indian land, but also taxation of the leasehold or possessory interest, and taxation of activities (e.g., excise or severance taxes) occurring or services performed on leased Indian land.

Tribes have inherent plenary and exclusive power over their citizens and territory, which has been subject to limitations imposed by Federal law, including but not limited to Supreme Court decisions, but otherwise may not be transferred except by the tribe affirmatively granting such power. *See, Cohen's Handbook of Federal Indian Law,* 2012 Edition, § 4.01[1][b]. The U.S. Constitution, as well as treaties entered into between the United States and Indian tribes, executive orders, statutes, and other Federal laws recognize tribes' inherent authority and power of self-government. *See, Worcester v. Georgia,* 31 U.S. 515 (1832); *U.S. v. Winans,* 198 U.S. 371, 381 (1905)("[T]he treaty was not a grant of rights to the Indians, but a grant of rights from them – a reservation of those not granted."); *Cohen's Handbook of Federal Indian Law,* 2012 Edition, § 4.01[1][c] ("Illustrative statutes… include [but are not limited to] the Indian Civil Rights Act of 1968, the Indian Financing Act of 1974, the Indian Self-Determination and Education Assistance Act of 1975… [and] the Tribe Self-Governance Act… In addition, congressional recognition of tribal authority is [also] reflected in statutes requiring that various administrative acts of… the Department of the Interior be carried out only with the consent of the Indian tribe, its head of government, or its council."); *Id.* ("Every recent president has affirmed the governmental status of Indian nations and their special relationship to the United States").

With a backdrop of "traditional notions of Indian self-government," Federal courts apply a balancing test to determine whether State taxation of non-Indians engaging in activity or owning property on the reservation is preempted. *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136, 143 (1980). The *Bracker* balancing test requires a particularized examination of the relevant State, Federal, and tribal interests. In the case of leasing on Indian lands, the Federal and tribal interests are very strong.

The Federal statutes and regulations governing leasing on Indian lands (as well as related statutes and regulations concerning business activities, including leases, by Indian traders) occupy and preempt the field of Indian leasing. The Federal statutory scheme for Indian leasing is comprehensive, and accordingly precludes State taxation. In addition, the Federal regulatory scheme is pervasive and leaves no room for State law. Federal regulations cover all aspects of leasing:

- Whether a party needs a lease to authorize possession of Indian land;
- How to obtain a lease;
- How a prospective lessee identifies and contacts Indian landowners to negotiate a lease;
- Consent requirements for a lease and who is authorized to consent;
- What laws apply to leases;
- Employment preference for tribal members;
- Access to the leased premises by roads or other infrastructure;
- Combining tracts with different Indian landowners in a single lease;
- Trespass;
- Emergency action by us if Indian land is threatened;

- Appeals;
- Documentation required in approving, administering, and enforcing leases;
- Lease duration;
- Mandatory lease provisions;
- Construction, ownership, and removal of permanent improvements, and plans of development;
- Legal descriptions of the leased land;
- Amount, time, form, and recipient of rental payments (including non-monetary rent), and rental reviews or adjustments;
- Valuations;
- Performance bond and insurance requirements;
- Secretarial approval process, including timelines, and criteria for approval of leases;
- Recordation;
- Consent requirements, Secretarial approval process, criteria for approval, and effective date for lease amendments, lease assignments, subleases, leasehold mortgages, and subleasehold mortgages;
- Investigation of compliance with a lease;
- Negotiated remedies;
- Late payment charges or special fees for delinquent payments;
- Allocation of insurance and other payment rights;
- Secretarial cancellation of a lease for violations; and
- Abandonment of the leased premises.

The purposes of residential, business, and WSR leasing on Indian land are to promote Indian housing and to allow Indian landowners to use their land profitably for economic development, ultimately contributing to tribal well-being and self-government. The legislative history of section 415 demonstrates that Congress intended to maximize income to Indian landowners and encourage all types of economic development on Indian lands. *See* Sen. Rpt. No. 84-375 at 2 (May 24, 1955). Assessment of State and local taxes would obstruct Federal policies supporting tribal economic development, self-determination, and strong tribal governments. State and local taxation also threatens substantial tribal interests in effective tribal government, economic self-sufficiency, and territorial autonomy. The leasing of trust or restricted land is an instrumental tool in fulfilling "the traditional notions of sovereignty and [] the federal policy of encouraging tribal independence." *Bracker*, 448 U.S. at 145 (citing *McClanahan v. Arizona State Tax Comm'n*, 411 U.S. 164, 174-75 (1973)). The leasing of trust or restricted lands facilitates the implementation of the policy objectives of tribal governments through vital residential, economic, and governmental services. Tribal sovereignty and self-government are substantially promoted by leasing under these regulations, which require significant deference, to the maximum extent possible, to tribal determinations that a lease provision or requirement is in its best interest. *See* Joseph P. Kalt and Joseph William Singer, The Native Nations Institute for Leadership, Management, and Policy & The Harvard Project on American Indian Economic Development, Joint Occasional Papers on Native Affairs, *Myths and Realities of Tribal Sovereignty: The Law and Economics of Indian Self-Rule*, No. 2004-03 (2004) ("economically and culturally, sovereignty is a key lever that provides American Indian communities with institutions

and practices that can protect and promote their citizens interests and well-being [and] [w]ithout that lever, the social, cultural, and economic viability of American Indian communities and, perhaps, even identities is untenable over the long run").

Another important aspect of tribal sovereignty and self-governance is taxation. Permanent improvements and activities on the leased premises and the leasehold interest itself may be subject to taxation by the Indian tribe with jurisdiction over the leased property. The Supreme Court has recognized that "[t]he power to tax is an essential attribute of Indian sovereignty because it is a necessary instrument of self-government and territorial management." *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130, 137 (1982). State and local taxation of lessee-owned improvements, activities conducted by the lessee, and the leasehold interest also has the potential to increase project costs for the lessee and decrease the funds available to the lessee to make rental payments to the Indian landowner. Increased project costs can impede a tribe's ability to attract non-Indian investment to Indian lands where such investment and participation are critical to the vitality of tribal economies. An increase in project costs is especially damaging to economic development on Indian lands given the difficulty Indian tribes and individuals face in securing access to capital. A 2001 study by the U.S. Department of the Treasury found that Indians' lack of access to capital and financial services is a key barrier to economic advancement. U.S. Dept. of the Treasury, Community Development and Financial Institutions Fund, The Report of the Native American Lending Study at 2 (Nov. 2001). Along the same line, 66 percent of survey respondents stated that private equity is difficult or impossible to obtain for Indian business owners. *Id.*

In many cases, tribes contractually agree to reimburse the non-Indian lessee for the expense of the tax, resulting in the economic burden of the tax ultimately being borne directly by the tribe. Accordingly, the very possibility of an additional State or local tax has a chilling effect on potential lessees as well as the tribe that as a result might refrain from exercising its own sovereign right to impose a tribal tax to support its infrastructure needs. Such dual taxation can make some projects less economically attractive, further discouraging development in Indian country. Economic development on Indian lands is critical to improving the dire economic conditions faced by American Indians and Alaska Natives. The U.S. Census Report entitled *We the People: American Indians and Alaska Natives in the United States*, issued February 2006, documented that a higher ratio of American Indians and Alaska Natives live in poverty compared to the total population, that participation in the labor force by American Indians and Alaska Natives was lower than the total population, and that those who worked full-time earned less than the general population.

162.017(a). Subject only to applicable Federal law, permanent improvements on trust or restricted land are not taxable by States or localities, regardless of who owns the improvements. Permanent improvements are, by their very definition, affixed to the land. Accordingly, a property tax on the improvements burdens the land, particularly if a State or local government were to attempt to place a lien on the improvement. Numerous provisions in the regulations address all aspects of improvements, requiring the Secretary to ensure himself that adequate consideration has been given to the enumerated factors under section 415(a). These include the height, safety, and quality of improvements; provisions requiring the lease to address ownership, construction, and removal of

improvements; provisions imposing due diligence requirements on the construction of improvements, and provisions requiring plans of development for business and WSR leases. *See, e.g.,*162.314 through 162.316, 162.414 through 162.416, 162.514 through 162.516, and 162.543 through 162.545. In addition, the regulations require the BIA to comply with tribal law, including tribal laws regulating improvements, when making decisions concerning leases of trust or restricted land. *See* 162.016. State and local taxation of improvements undermine Federal and tribal regulation of improvements.

162.017(b). Subject only to applicable Federal law, activities conducted under a lease of trust or restricted land that occur on the leased premises are not taxable by States or localities, regardless of who conducts the activities. An example of this principle is in the trading business where the courts have held that taxation of such activities is preempted by the Indian Trader Statutes, *see* 25 U.S.C. 261, and the all-inclusive regulations under them, *see* 25 CFR 140.1-.26. Federal statutes and regulations are "sufficient to show that Congress has taken the business of Indian trading on reservations so fully in hand that no room remains for State laws imposing additional burdens upon traders." *Warren Trading Post Co. v. Arizona State Tax Comm'n,* 38 U.S. 685, 690 (1995) (precluding imposition of State sales taxes); *Central Machinery Co. v. Arizona State Tax Comm'n,* 448 U.S. 160 (1980) (preemption applies even if vendor is not licensed as long as goods or services are traded to a tribe or its members in a transaction occurring predominately on the reservation). As a general matter, myriad activities on leased lands related to economic development, infrastructure building, and governmental operations provide important revenue and services to the tribal economy and the generation of economic activity on leased land is an essential component of tribal self-

sufficiency. State and local taxation undermines that important objective of federal regulation of the leasing of Indian lands. This subsection, like 162.017(a), is intended to achieve the dual purposes of supporting tribal economic development and promoting tribal self-government. The additional burden of State and local taxation on lease activities would significantly affect the marketability of Indian land for economic development, as noted above in the introductory paragraphs. In addition, tribes, as sovereigns, have inherent authority to regulate zoning and land use on Indian trust and restricted land, and the regulations require BIA to comply with tribal laws relating to land use. *See* 162.016. Such regulation is undermined by State and local taxation.

162.017(c). Subject only to applicable Federal law, the leasehold or possessory interest itself is not taxable by States or local governments. The ability of a tribe or individual Indian to convey an interest in trust or restricted land arises under Federal law, not State law; Federal legislation has left the State with no duties or responsibilities for such interests, even recordation (25 U.S.C. 5); and the leasehold interest is exhaustively regulated by this rule, as noted above. For example, a leasehold interest may not be conveyed, mortgaged, assigned, or subleased without Secretarial approval, with limited exceptions. Compelling Federal interests in self-determination, economic self-sufficiency, and self-government, as well as strong tribal interests in sovereignty and economic self-sufficiency, are undermined by State and local taxation of the leasehold interest.

Nothing in these regulations is intended to preclude tribes, States, and local governments from entering into cooperative agreements to address these taxation issues, and in fact, the Department strongly encourages such agreements.

In addition, we received the following comments:

- Move the language regarding the justification for the taxation provisions to the regulatory text. We did not make this change because the justification is explanatory and therefore more appropriate in the preamble than in the regulatory text.
- Correct the ambiguity caused by the location of the phrase "without regard to ownership" in the proposed rule, because it could be construed as describing the State tax such that the section would bar only those State taxes imposed without regard to ownership of the improvements. Because that interpretation was not the intent of this provision, we have clarified the provision by moving the phrase "without regard to ownership" to indicate that no improvements on leased Indian land are subject to State taxation, regardless of who owns the improvements.
- Delete the language following the provision stating that improvements are subject to 25 CFR 1.4. We deleted the cross-reference to 25 CFR 1.4 and instead added the crux of section 1.4 directly into 162.014.

162.018 (PR 162.015) – Tribal Administration of Part 162

- Clarify the phrase "inherent Federal function." We accepted this comment by deleting the phrase and instead providing a list of functions that cannot be contracted or compacted by tribes in the leasing context.

162.019 (PR 162.016) – Access to Leased Premises

- Exempt roads and other infrastructure lease provisions from requiring part 169 approval where the access is incidental to the development and use of the leased lands. Rights-of-way across Indian land require Secretarial approval, by statute. If access to the

(2) The Indian landowners expressly agree to the application of State or local law.

(d) An agreement under paragraph (c) of this section does not waive a tribe's sovereign immunity unless the tribe expressly states its intention to waive sovereign immunity in the lease of tribal land.

§ 162.015 May a lease contain a preference consistent with tribal law for employment of tribal members?

A lease of Indian land may include a provision, consistent with tribal law, requiring the lessee to give a preference to qualified tribal members, based on their political affiliation with the tribe.

§ 162.016 Will BIA comply with tribal laws in making lease decisions?

Unless contrary to Federal law, BIA will comply with tribal laws in making decisions regarding leases, including tribal laws regulating activities on leased land under tribal jurisdiction, including, but not limited to, tribal laws relating to land use, environmental protection, and historic or cultural preservation.

§ 162.017 What taxes apply to leases approved under this part?

(a) Subject only to applicable Federal law, permanent improvements on the leased land, without regard to ownership of those improvements, are not subject to any fee, tax, assessment, levy, or other charge imposed by any State or political subdivision of a State. Improvements may be subject to taxation by the Indian tribe with jurisdiction.

(b) Subject only to applicable Federal law, activities under a lease conducted on the leased premises are not subject to any fee, tax, assessment, levy, or other charge (e.g., business use, privilege, public utility, excise, gross revenue taxes) imposed by any State

or political subdivision of a State. Activities may be subject to taxation by the Indian tribe with jurisdiction.

(c) Subject only to applicable Federal law, the leasehold or possessory interest is not subject to any fee, tax, assessment, levy, or other charge imposed by any State or political subdivision of a State. Leasehold or possessory interests may be subject to taxation by the Indian tribe with jurisdiction.

§ 162.018 May tribes administer this part on BIA's behalf?

A tribe or tribal organization may contract or compact under the Indian Self-Determination and Education Assistance Act (25 U.S.C. 450f et seq.) to administer any portion of this part that is not an approval or disapproval of a lease document, waiver of a requirement for lease approval (including but not limited to waivers of fair market rental and valuation, bonding, and insurance), cancellation of a lease, or an appeal.

§ 162.019 May a lease address access to the leased premises by roads or other infrastructure?

A lease may address access to the leased premises by roads or other infrastructure, as long as the access complies with applicable statutory and regulatory requirements, including 25 CFR part 169. Roads or other infrastructure within the leased premises do not require compliance with 25 CFR part 169 during the term of the lease, unless otherwise stated in the lease.

§ 162.020 May a lease combine tracts with different Indian landowners?

(a) We may approve a lease that combines multiple tracts of Indian land into a unit, if we determine that unitization is:

(1) In the Indian landowners' best interest; and