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Via U.S. Mail and Facsimile

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RE: Turn-key Facility Development Agreement, Loan Agreement, Security Agreement, Tribal Agreement, Pre-Development Note, and Temporary Facility Note between the Wyandotte Nation of Oklahoma and Kansas Gaming Ltd. and AHG Group LLC

Dear Chief Bearskin and Messrs. Pontiere, Sawruk, Ginsburg, and Harris:

On January 22, 2008, National Indian Gaming Commission (NIGC) field investigators forwarded for review a package of six agreements between the Wyandotte Nation of Oklahoma (Nation) and Kansas Gaming Ltd. (KG) and AHG Group LLC (AHG). Those agreements are:

1. The Turn-Key Development Agreement (DA) between the Nation and KG (May 21, 2007);
2. The Loan Agreement (LA) between the Nation and AHG (May 21, 2007);

3. The Security Agreement (SA) between the Nation and both KG and AHG (May 21, 2007);
4. The Tribal Agreement (TA) containing general covenants between the Nation and both KG and AHG (May 21, 2007);
5. The Pre-Development Note between the Nation and KG (May 21, 2007); and
6. The Temporary Facility Note between the Nation and KG (May 21, 2007). (Collectively, "the agreements.")

Under the agreements, KG promises to assist the Nation by constructing and furnishing a turn-key gaming operation. AHG will provide the bridge financing. KG specifically promises the following:

1. Finding a permanent lender for construction financing,
2. Designing and constructing the turn-key gaming operation, and
3. Finding and installing machines that the Nation chooses.

See Turn-key facility development agreement between Wyandotte Gaming Enterprise and Kansas Gaming Ltd. (DA) (May 21, 2007) Recital I. Generally, KG promises to do whatever is required and necessary to get the facility up and running for the Nation.

After reviewing the agreements, it is my opinion that both the DA and the LA are management contracts within the meaning of the Indian Gaming Regulatory Act (IGRA), 25 U.S.C. § 2701 et seq., and therefore must be submitted to and approved by the NIGC Chairman. 25 U.S.C. § 2711. Furthermore, these two agreements violate IGRA's sole proprietary interest mandate. 25 U.S.C. § 2710(b)(2)(A); 25 C.F.R. § 522.4(b)(1). As such, it is my opinion that the DA and the LA are void. The parties must revise the agreement immediately and address the issues identified in this opinion. Otherwise, we will refer this agreement to the Director of Contracts and the Director of Enforcement for their review.

Authority

The authority of the NIGC to review and approve gaming-related contracts is limited by IGRA to management contracts and collateral agreements to management contracts to the extent that they implicate management. *Catskill Development LLC v. Park Place Entertainment Corp.*, No. 06-5860, 2008 U.S. App. Lexis 21839 at *38 (2nd Cir. October 21, 2008) ("a collateral agreement is subject to agency approval under 25 C.F.R. § 533.7 only if it 'provides for management of all or part of a gaming operation.'"); *Machal Inc. v. Jena Band of Choctaw Indians*, 387 F. Supp. 2d 659, 666 (W.D. La. 2005) ("collateral agreements are subject to approval by the NIGC, but only if that agreement 'relate[s] to the gaming activity'"). *Accord*, *Jena Band of Choctaw Indians v. Tri-Millenium Corp.*, 387 F. Supp. 2d 671, 678 (W.D. La. 2005); *United States ex rel. St. Regis Mohawk Tribe v. President R.C.-St. Regis Management Co.*, No. 7:02-CV-845, 2005 U.S. Dist. LEXIS 12456, at *3-*4, *9-*10 (N.D.N.Y. June 13, 2005), *aff'd on other grounds*, 451 F.3d 44 (2nd Cir. 2006).

The NIGC has defined the term *management contract* as "any contract, subcontract, or collateral agreement between an Indian tribe and a contractor or between a contractor and a subcontractor if such contract or agreement provides for the management of all or part of a gaming operation." 25 C.F.R. § 502.15. *Collateral agreement* is defined as "any contract, whether or not in writing, that is related either directly or indirectly, to a management contract, or to any rights, duties or obligations created between a tribe (or any of its members, entities, organizations) and a management contractor or subcontractor (or any person or entity related to a management contractor or subcontractor)." 25 C.F.R. § 502.5.

Though NIGC regulations do not define *management*, the term has its ordinary meaning. Management encompasses activities such as planning, organizing, directing, coordinating, and controlling. *NIGC Bulletin No.* 94-5: "Approved Management Contracts v. Consulting Agreements (Unapproved Management Contracts are Void)." Accordingly, the definition of *primary management official* is "any person who has the authority to set up working policy for the gaming operation." 25 C.F.R. § 502.19(b)(2). Further, management employees are "those who formulate and effectuate management policies by expressing and making operative the decision of their employer." *N.L.R.B. v. Bell Aerospace Co.*, 416 U.S. 267, 288 (1974). Whether particular employees are "managerial" is not controlled by an employee's job title. *Waldo v. M.S.P.B.*, 19 F. 3d 1395 (Fed. Cir. 1994). Rather, the question must be answered in terms of the employee's actual job responsibilities, authority, and relationship to management. *Id.* at 1399. In essence, an employee can qualify as management if the employee actually has authority to take discretionary actions – a *de jure* manager – or recommends discretionary actions that are implemented by others possessing actual authority to control employer policy – a *de facto* manager. *Id.* at 1399 *citing N.L.R.B. v. Yeshiva*, 444 U.S. 672, 683 (1980).

If a contract requires the performance of any management activity with respect to all or part of a gaming operation, the contract is a management contract within the meaning of 25 U.S.C. § 2711 and requires the NIGC Chairman's approval. Management contracts not approved by the Chairman are void. 25 C.F.R. § 533.7.

Management Contract Discussion

Notwithstanding the intent expressed in the LA that "the Lender acknowledges and agrees . . . that it has not, nor shall it assert, any rights to manage the facility," the default remedies in both the DA and the LA grant certain management powers. *See* LA § 8.26. DA § 11.3.1.2 states:

> The Gaming Enterprise . . . agrees that the security interest granted Developer in and to the Pledged Revenues and the Equipment is Developer's sole and exclusive security for the performance of the obligations . . . In order not to defeat the purpose of the Tribe's grant of such security interest to Developer, the Gaming Enterprise . . . expressly appoints Developer as its attorney-in-fact for purposes of this Section

> 11.3.1.2. Upon the occurrence of an uncured Event of Default, Developer, as attorney-in-fact . . . shall request that a court of competent jurisdiction, as specified . . . enter an order (i) appointing a receiver, trustee or custodian who shall ensure that the Pledged Revenues are transferred to the Depository on a daily basis, payment or allocation of the Pledge Revenues . . . in accordance with the Transaction Documents, and the maintenance of the Equipment. DA § 11.3.1.2.

Likewise, the LA permits the Lender to "exercise or enforce any all other rights or remedies available under any of the Loan Documents." LA § 7.1(c)(iii). This arrangement incorporates the remedy listed above in the DA.

In other words, both the DA and the LA permit KG and AHG to request a receiver in the event of an uncured default and that person will control, and by definition manage, the Pledged Revenues. A receiver is:

> A person appointed by a court for the purpose of preserving property of a debtor . . . to receive and preserve the property . . . and receive its rents, issues, and profits, and apply or dispose of them at the direction of the court . . . . *See* BLACK'S LAW DICTIONARY 1268 (6th ed. 1990).

A receiver does not hold title to the properties at issue but does handle the financial transactions involved. *Id.* It is up to a court's discretion to appoint a receiver. *See* Elaine Panagakos and Peter Klarfeld, *Franchisees in Federal Receivership: Strategic Considerations for Franchisors*, 26 FRANCHISE L.J. 79, 79 (2006). More specifically, a court's decision here to appoint a receiver would bring the property within the custody and control of the court – and takes it away from the Nation. *Id.* at 79. In short, a court would bestow upon the receiver a "broad authority over management of the property." *Id.*; *see also S.E.C. v. Capital Consultants LLC*, 397 F.3d 733, 738 (9th Cir. 2005).

In this instance, the receiver would have the power to manage the Pledged Revenues in the event of default, and this would include management authority and control over the casino's operating expenses – control that is management within the meaning of IGRA. *See* DA § 11.3.1.2; *see also* LA § 7.1(c)(iii).

The term *Pledged Revenues* is defined as: "For any given day, the Pledged Revenues shall equal the Gross Revenue for that day less the Daily Cash Requirements for that day." *See* Master Definitions List, Exhibit A. The term *Daily Cash Requirements* is defined as: "The amount of cash which the General Manager determines . . . the Gaming Enterprise will keep on hand on a daily basis within the Facility." *Id.* The daily cash requirement is the money required to keep the operation open for a day, such as prize payouts, and it constitutes the bankroll for the operation. This does not cover all potential expenses that can be deemed operating expenses. Therefore, while the money set aside to meet the casino's daily obligations to its patrons is not part of *Pledged Revenues* controlled by the receiver, operating expenses are. The receiver "stands in the shoes" of the Nation for purposes of controlling the revenue, and thus, control of revenue,

including operating revenue, would be outside the Nation. 65 AM.JUR.2D *Receivers* § 105; *see also Jarvis v. Technical Land, Inc.* 172 B.R. 429, 431-32 (B.R.D.C. 1994). This grant of authority usurps management of certain parts of the gaming operation from the Nation.

To alleviate any concerns regarding this issue, I advise the parties to craft limiting language for what constitutes Pledged Revenues and limiting language on the powers of any third party in the event of default.

Proprietary Interest

Among IGRA's requirements for approval of tribal gaming ordinances is that "the Indian tribe will have the sole proprietary interest and responsibility for the conduct of any gaming activity." 25 U.S.C. § 2710(b)(2)(A). Under this provision, if any entity other than a tribe possesses a proprietary interest in the gaming activity, gaming may not take place. NIGC regulations also require that all tribal gaming ordinances include such a provision. 25 C.F.R. § 522.4(b)(1).

Although there are no cases directly on point, courts have defined *proprietary interest* in a number of contexts. In a criminal tax case, an appellate court discussed what the phrase *proprietary interest* meant, after the trial court had been criticized for not defining it for jurors, saying:

> It is assumed that the jury gave the phrase its common, ordinary meaning, such as 'one who has an interest in, control of, or present use of certain property.' Certainly, the phrase is not so technical, nor ambiguous, as to require a specific definition.

Evans v. United States, 349 F.2d 653 (5th Cir. 1965). In another tax case, *Dondlinger v. United States*, 1970 U.S. Dist. LEXIS 12693 (D. Neb. 1970), the issue was whether the plaintiff had a sufficient proprietary interest in a wagering establishment to be liable for taxes assessed against persons engaged in the business of accepting wagers. The court observed:

> It is not necessary that a partnership exist. It is only necessary that a plaintiff have some proprietary interest. . . One would have a proprietary interest if he were sharing in or deriving profit from the club as opposed to being a salaried employee merely performing clerical and ministerial duties.

Id. (emphasis added). The legislative history of IGRA is an additional aid for interpreting the statute's mandate that a tribe "have the sole proprietary interest and responsibility for the conduct of any gaming activity." 25 U.S.C. § 2710(b)(2)(A). The legislative history of the IGRA states that "the tribe must be the sole owner of the gaming enterprise." S. Rep. 100-446, 1988 U.S.C.C.A.N. 3071- 3078.

Finally, in regulatory preamble language, the NIGC provided a non-exhaustive list of arrangements that would violate the sole proprietary interest clause. According to this published guidance, sole proprietary interest violations would exist under:

- an agreement whereby a vendor pays the tribe for the right to place gambling devices that are controlled by the vendor on the gaming floor;
- a security agreement whereby a tribe grants a security interest in the gaming operation, if such an interest would give a party other than the tribe the right to control gaming in the event of default by the tribe; and
- stock ownership in a tribal gaming operation, even by tribal members.

58 Fed. Reg. 5802, 5804 (Jan. 22, 1993). Again, this list was not meant to be exhaustive, but it does provide three types of scenarios that are not allowed under IGRA's sole proprietary interest clause.

Proprietary Interest Discussion

I am concerned that KG's fees for its services under the DA violate IGRA's sole proprietary interest mandate because they do not appear to be reasonably related to the service provided. Development fees that are tied to the operation's profits and fail to reasonably relate to the service provided, or the risk undertaken, can look more like a stake in the business rather than mere payment for services rendered. Payment by taking a percentage interest can also indicate that the contractor, as well as the tribe, has an ownership interest in the profits of the gaming operation. As the typical fee runs between 2-5% of development costs for a developer, a higher fee would require justification through special risks or duties. Special risks or duties often evidence reasonable compensation for special services and benefits provided to the Nation. Absent such duties or risks, a higher than standard fee would connote a proprietary interest that violates IGRA. The Office of General Counsel opines that any risk perceived must be proportional or reasonably related to the fee.

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KG will receive [ ] gross revenues from the project. DA § 5.3.2. KG expects to receive this fee for [ ] years after the gaming operation opens. *Id.* at § 4.1. In fact, [ ] gross revenues equals [ ] of net income, based on the gaming operation's profits and costs over the last year. That is more than twice the amount a manager may receive under an NIGC approved management contract. The figures below are based on the actual figures presented from the gaming operation's audit.

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Because the development costs for the facility were [redacted] and the industry standard of payment hovers around 5% of development costs, a typical fee for this project is only [redacted] for the contract's duration. However, the figures indicate that KG is making twice that amount in one year. Put another way, the developer is receiving over [redacted] net revenue annually for its work for the next [redacted]. If these figures remain constant over the duration of the contract, then KG will profit from this arrangement [redacted] more than the industry standard.

KG does identify additional risks in the DA that may help explain its fee. KG cites the following risks as reasons for its higher fee:

1. Changes to applicable gaming laws,
2. Changes to tribal laws,
3. Shifts in tribal politics,
4. Challenges to the Tribe's right to game in the area,
5. Rulings by governmental authorities adverse to the deal,

6. Inaccuracies in covenants, warranties, and representations, and
7. Competition from other tribes.

See Development agreement § 5.1.3.

However, a risk requires an element of uncertainty in the undertaking. BLACK'S LAW DICTIONARY at 1328. If the uncertainty does not remain, then neither does the risk.

KG states that changes to federal, state, or tribal law constitute risks. Political upheavals and changes to laws could sour the deal and justify a higher fee. But these are not unique risks to this contract or any other agreement in Indian Country and do not justify an increased fee. Likewise, potential changes in tribal administration are not unique. Further, the Nation promises to neither pass nor amend any law in such a way as to adversely affect the deal. *See* Tribal agreement between Wyandotte Gaming Enterprise, the Wyandotte Nation, and Kansas Gaming, Ltd. (May 21, 2007). This contractual promise binds the leadership, so this precaution should satisfy any concerns about legal or political upheavals in the Nation. As the Nation agrees not to undercut the deal, this is no unique risk to justify a higher fee.

In its fourth and fifth risks, KG states that third-party challenges and adverse rulings from government agencies pose risks that justify a higher fee. We assume that KG refers to *Sac & Fox v. Kempthorne,* 2008 U.S. Dist. LEXIS 69599 (D. Kan. Sept. 10, 2008) and its associated cases.

The deal presented here was signed on May 21, 2007, over one year after the District Court in Kansas affirmed the Secretary of the Interior's decision to take the Shriner Tract into trust. *See Governor of Kansas v. Norton,* 430 F. Supp. 2d 1204, 1207 (D. Kan. May 9, 2006). The Governor of Kansas appealed this decision, and at the time of this contract's execution, that appeal was pending.

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Thus, while there was some risk posed by this litigation at the time of this contract's execution, it does not justify taking [redacted] net revenue for almost [redacted] ears. The Nation had received a positive decision approving the Secretary's decision to take the land into trust. An appeal of the decision from the opposition was an uphill battle, as are most appeals.

Further, the limited nature of the risk was in fact borne out by subsequent events. The Tribe continued to succeed in its litigation. The federal government took the land into trust and the Quiet Title Act barred challenges to the completed trust acquisition of the Shriner Tract. In October 2007, six months after the contract was signed, the Tenth Circuit dismissed the appeal for lack of jurisdiction under the Quiet Title Act. *Governor of Kansas v. Kempthorne*, 505 F.3d 1089, 1092 (10th Cir. Oct. 24, 2007). The Nation has consistently won every round of litigation on the matter. The Sac & Fox Nation attempted to vacate the district court decision but the court dismissed this last attempt to challenge the land's status. *See generally Sac & Fox,* 2008 U.S. Dist. LEXIS 69599. An appeal is pending before the Tenth Circuit, but success appears unlikely.

Finally, KG states that potential misrepresentations and competition from other tribes necessitate a higher fee. As to misrepresentation, the agreement makes enforceable the Nation's covenants to the developer. *See* Development agreement §§ 10.4-10.7. As to competition, it is true that the operation contains only [redacted] machines and competes with downtown riverboats for business. *See* Rick Alm, *Tribal-owned casino opens in downtown KCK*, KansasCity.com, http://newsok.com/article/3191382/?print=1 (last visited February 4, 2008). This risk, however, cannot justify taking [redacted] gross revenue from the Nation for almost [redacted] years. Risks such as this run throughout Indian country and do not necessitate a fee of this magnitude. A fee that takes over [redacted] of the Nation's net gaming revenue for almost [redacted] years cannot be justified by standard risks taken in a competitive market. Something more is needed.

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In sum, absent any other explanation for the developer taking such a substantial share of the casino's net revenue, I am left to conclude that the developer is effectively taking an ownership interest in the property for the next [redacted] years, and this violates the sole proprietary interest mandate in IGRA.

Conclusion

The default remedy regarding the security interest in the DA and the LA make these agreements management contracts within the meaning of 25 U.S.C. § 2711. Also, the fees in the DA violate the sole proprietary interest mandate of IGRA. The parties must revise these agreements immediately. Otherwise, we will refer the matter to the Director of Contracts and the Director of Enforcement for their review.

Sincerely,

Penny J Coleman

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