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March 14, 1985

This is in reply to your letter of January 16, 1985 to Thad Gembacz in which you request that we review the Management Agreement between (Owner) and the Company (Contractor-Manager) and the taxpayer's points and authorities in support of the contention that no possessory interest was created by the Management Agreement. Since the date of the Management Agreement, September 29, 1982, the Company has assigned its interest in the Agreement to P , a Texas corporation.

The first point raised by P in support of its contention is that as a result of government policy, legislation and judicial opinion, Indians are free to make their own laws and be governed by them on reservations in disregard of civil regulations that bind non-Indians. Thus, argues P , neither the State nor the County has authority over Indian bingo and therefore no right to tax the bingo operation. P cites several federal cases in support of its contention.

First, it should be made clear that it is not the bingo operation that is being taxed, but rather a possessory interest in the real property used for the bingo operation. Moreover, none of the cases cited by P in support of its first point deal with the question of imposing property tax on a possessory interest on the use by non-Indians of federal land held in trust for Indians. In fact, the courts have upheld such taxation. Palm Springs Spa, Inc. v. Riverside County (1971) 18 Cal.App.3d 372; Agua Caliente Band of Mission Indians v. Riverside County (1971) 442 F. 2d 1184, cert. denied 405 U.S. 933; Fort Mojave Tribe v. San Bernardino County (1976) 543 F. 2d

1253, cert. denied 430 U.S. 983. In the latter case, the court held among other things that the imposition of a possessory interest tax on non-Indian lessees of land held in trust for the Fort Mojave Indian Tribe was not invalid as being an interference with the tribe's right of self government.

2. P next argues that federal law provides that any conveyance of any interest in tribal real property is null and void without the approval of the Secretary of the Interior and that since "the Secretary of the Interior did not approve the contract as a possessory interest", no possessory interest can legally exist. P assertion that the Secretary "did not approve the contract as a possessory interest" suggests that the Secretary may have in fact approved the Management Agreement as a contract as required by federal law. Since a possessory interest may be created by a contract other than a lease, (18 Cal. Admin. Code Sec. 21(a)(1)), there may be no problem of validity.

In any event, P argument assumes that a taxable possessory interest cannot exist in the absence of a valid instrument of conveyance such as a lease approved by the Secretary of the Interior. Such an assumption is contrary to California law as explained by the California Supreme Court in the early case of People v. Shearer (1866) 30 Cal. 645. In that case, Shearer adversely possessed federal land for farming purposes and also added valuable improvements to the land. The court concluded that Shearer's occupancy, standing alone, resulted in a taxable interest recognizing that the mere right to use and possess the property was a "valuable species of property". The court stated at page 655:

> "The possession itself of the public lands and the improvements thereon, whether by naked trespassers, or those who claim in addition a right of pre-emption, as to everybody except the United States, have always in California,...been regarded as valuable property interests." (Emphasis added.)

The court further stated at page 657:

> "It is not the land itself, nor the title to the land,...It is not the pre-emption right, but it is the possession and valuable use of the land subsisting in the citi-

> zen. Why should it not contribute its proper share, according to the value of the interest,...of the taxes necessary to sustain the Government which recognizes and protects it?"

(See also 18 Cal. Admin. Code Sec. 21(a)(2).)

From the foregoing, it thus seems clear that it is the fact of possession and valuable use that is crucial in determining the existence of a taxable possessory interest and not necessarily whether the instrument under which the possession and valuable use are exercised is valid.

3. The next contention made by P is that it has a true management contract with the Indian tribe and has not been granted a concession to operate bingo games and does not have possession of the real property.

In determining the existence of a possessory interest, the situation must be measured by an objective standard rather than by accepting the literal language of the written instrument as controlling the nature of the relationship established. Stadium Concessions, Inc. v. City of Los Angeles (1976) 60 Cal.App.3d 215. In Mattson v. County of Contra Costa (1968) 258 Cal.App.2d 205, the court described the objective standard by which the presence or absence of a possessory interest can be determined as follows:

> "The agreement refers to respondents as concessionaires, and does not use the words 'lessees' or 'tenants'. But the descriptive words used are not controlling...In arrangements of the general nature of the one before us, to which a unit of government is a party, almost inevitably there are some features of relative durability, independence, exclusiveness and fixedness, and others of relative impermanence, subjection to control and public participation. In each case, judgment must be made by examination of the agreement in its entirety." (Mattson, supra, 258 Cal.App.2d 205, at pp. 207, 209.)

From the foregoing, it is clear that the designation of the Agreement as a " Management Agreement" and

P as a "Contractor-Manager" rather than a lessee or concessionaire are not controlling. In applying the objective standard set forth in Mattson, there appears to be no dispute regarding relative durability. The Agreement calls for a 15 year term and has been in effect for more than two years. The Agreement may only be terminated by mutual consent or by the Owner in the event the Contractor-Manager is found guilty of theft or embezzlement or is found guilty of a material breach of the Agreement in a court of competent jurisdiction. (Par. VIII.) This provision is qualified to the extent that if an employee of the Contractor-Manager is found guilty of theft or embezzlement, it shall not be grounds for termination provided the Contractor-Manager repays the funds due the Owner. The requirement of relative durability is therefore satisfied.

The factor of fixedness is satisfied by the provisions of paragraph VII (pages 10 and 11) and P raises no issue regarding this factor.

With respect to the factor of relative exclusiveness, the Agreement provides (Page 2) that "Owner is desirous of vesting in Contractor-Manager, the exclusive right and obligation to finance, construct, improve, develop, manage, operate and maintain the Property...and Contractor-Manager is desirous of performing the above described functions as exclusive Contractor of the Owner." It further provides (Par. I.2.) that "Owner hereby retains and engages CONTRACTOR-MANAGER...to act solely and exclusively...to construct, improve, develop, manage, operate and maintain the Property...as a facility for the conduct of bingo." (Emphasis added.) In addition, P is to provide all personnel, inventory and supplies necessary to operate and maintain the Property (Par. II.B.), and provide a Program Director who will act as General Manager for the Property and who will operate and manage the Property on a full-time basis (Par. II.F.1.). Based on the foregoing provisions, it hardly seems disputable that P has the exclusive right to use and possess the Property to whatever extent is necessary to conduct the bingo operation.

The remaining factor is that of relative independence and it is this factor that P , in effect, argues is non-existent. P claims it is a mere agent or employee of the Indian tribe.

P argues that if it is not an agent or employee of the Indian tribe and is instead a

concessionaire then Penal Code Section 326.5 is being violated citing Barona Group of Capitan Grande Band of Mission Indians v. Duffy (1982) 694 F. 2d 1185. From this Paland concludes that if Penal Code Section 326.5 is not applicable as Barona holds, there is no possessory interest.

Barona does not support P argument. That case simply held that county and state laws governing bingo (Penal Code Section 326.5) were civil and regulatory in nature, and, therefore, were not applicable on the Indian reservation. Thus, the exemption for Indian bingo was based on the fact that the bingo operation was located on the reservation and did not depend upon whether it was operated by an agent of the tribe or a concessionaire or independent contractor. Accordingly, contrary to P argument, P may have a possessory interest in the Property notwithstanding the inapplicability of Penal Code Section 326.5 to the bingo operation.

P next cites Pacific Grove-Asilomar Operating Corp. v. County of Monterey (1974) 43 Cal.App.3d 675 in support of its position that it is a mere agent or employee of the Indian tribe and that no possessory interest exists here. In that case, the court applied the objective standard set forth in Mattson and found that an agency was created by the agreement there in question.

The court concluded that Asilomar's management of the property was not independent, but subject to state control in every way. The court noted, however, that "the fact that the relationship between Asilomar and the state has no profit motive is an element material in determining the nature of Asilomar's interest." (Asilomar was a nonprofit corporation organized and established solely to manage the state-owned conference grounds in question and derived no private benefit from its management of the property.) The court also noted that Asilomar did not have exclusive use of the property since the property was open to the general public. In the commercial setting involved in Mattson, however, such public access (to the dining area of a public golf course operation) was held not to detract from the element of exclusiveness of possession. Mattson, supra, 258 Cal.App.2d 205, 210.

Since P is to receive 45 percent of the net operating profits each year, this case is clearly distinguishable from the Pacific Grove case. Moreover, the management agreement in that case listed 25 specific state controls which led to the court's conclusion that an agency relationship existed. Few such controls exist here. In fact, a comparison of the controls here with those in

Pacific Grove and Mattson indicates that the relationship here is more like that in Mattson than in Pacific Grove. In Mattson, as here, the hiring and firing of employees was up to the taxpayer. (Par. II.F.) 1/ In Mattson, as here, everything connected with the enterprise was under Mattson's management subject to limited controls. (Par. II.G.1.) 2/ If anything, the controls here are fewer and less stringent than those in Mattson. The court in Mattson characterized the operation in that case as "much too autonomous to be regarded as a mere agency." As indicated above, the level of control exercisable under the agreement in this case is much closer to that in Mattson than it is to the level of control in Pacific Grove. Accordingly, we are of the opinion that P is sufficiently independent of the control of the Indian tribe so as not to be considered a mere agent or employee.

P argues that it can't be a tenant or concessionaire because it pays no rent or fee but rather is "instead itself paid a fluctuating 'wage' depending on earnings from the operation."

It is true that under the Agreement, P is to receive as a management fee 45 percent of the net operating profits for each fiscal year (Par. IV.). That, of course,

1/ Employees - It is hereby understood and agreed that CONTRACTOR-MANAGER shall have the responsibility on behalf of OWNER to employ, direct, control and discharge all personnel performing regular services in and on the Property in connection with the construction, improvement, development, maintenance, operation and management of such Property, and any activity upon the Property; provided, however, CONTRACTOR-MANAGER shall give first preference to qualified members of the in hiring such personnel. Compensation for the services of such employees shall be considered an operating expense of the Property.

2/ All business and affairs in connection with the financing, construction, improvement, development, operation, management and maintenance of the Property subject to this Agreement shall be the responsibility of the CONTRACTOR-MANAGER, who is hereby granted necessary power and authority to act in order to fulfill its responsibility pursuant to this Agreement. Notwithstanding anything herein contained to the contrary, CONTRACTOR-MANAGER hereby agrees to and shall at all times comply with all terms and conditions of this Management Agreement in carrying out its responsibilities.

means that Owner receives 55 percent. Since P col-lects all gross revenues and deducts and pays the expenses from such gross revenues (Par. II.G.2.), and since determination of net operating profits available for distribution to the parties is determined in monthly intervals (Par. IV.C.), P , in effect, is paying Owner 55 percent of the net operating profits each month. Under typical concession agreements, the concessionaire pays a percentage of gross receipts as a rental (Pacific Grove, supra, at p. 692). The arrangement in this case is indistinguishable in effect from the typical concession agreement.

Further, there are several provisions in the Agreement that are virtually identical to the provisions of the agreement before the court in Sea-Land Service, Inc. v. County of Alameda (1974) 36 Cal.App.3d 837, which the court concluded made the agreement comparable to a lease:

The term is 15 years; the premises are clearly described; the permitted use is set forth with clarity ("conduct of bingo and other gaming activities", Par. I.); the compensation for such use is clearly stated; P is required to keep the premises neat, clean and orderly and is wholly responsible for repairs and maintenance (Par. V. a.); the Property is jointly insured by Owner and P (Par. VIII.1). Sea-Land Service, Inc. v. County of Alameda (1974) 36 Cal.App.3d 837, 842. Moreover, the Agreement contains a covenant against assignment without written consent (Par. VIII.2.) which, although not conclusive, "is frequently characteristic of leases and is inconsistent with mere license." (Mattson, supra, at p. 211.)

Finally, P argues that during consideration of a recent bill (H.R. 4566) which would have banned percentage payment by Indians on management contracts had it won passage, at no time was it suggested that percentage payment management agreements conveyed a possessory interest in Indian real property. Presumably, it was not suggested either that percentage payment management agreements did not convey possessory interests in Indian real property. Accordingly, all that P argument proves is that the issue of the existence or nonexistence of possessory interests never came up during consideration of H.R. 4566.

Based on our review of the Management Agreement, P legal arguments and the foregoing analysis, we disagree with P contention that it has no taxable

possessory interest in the real property operated as a bingo parlor.

Very truly yours,

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