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BEFORE THE
SENATE COMMITTEE ON INDIAN AFFAIRS

September 21, 2005

Good morning Chairman McCain, Vice-Chairman Dorgan, members of the Committee and staff. My name is Philip Hogen. I am the Chairman of the National Indian Gaming Commission (NIGC or Commission) and a member of the Oglala Sioux Tribe of the Pine Ridge Indian Reservation in South Dakota.

Thank you for the opportunity to discuss a matter of grave concern to the NIGC. As you are aware, a decision recently issued by the D.C. District Court found unlawful the NIGC's Minimum Internal Control Standards (MICS) regulations as applied to Class III gaming. Although the decision applies solely to the Colorado River Indian Tribes, the language of the decision is broadly worded and could be used in other forums to argue for the elimination of the NIGC's entire regulatory role in Class III gaming. While the challenge was with respect to the MICS regulations specifically, the District Court opinion contains language that appears to apply to all regulation of Class III gaming. One particularly troubling quotation from the opinion bears mention. The court stated, "[t]he [Indian Gaming Regulatory Act] not only lacks language giving the NIGC a role in the regulation of Class III gaming, but it contains several provisions that are inconsistent with such a role." Colorado River Indian Tribes v. Nat'l Indian Gaming Comm'n, No. 1:04-cv-00010-JDB, 2005 U.S. Dist. LEXIS 17722, at *34 (D.D.C. August 24, 2005). This statement by the court is troubling because it rejects the very clear "Declaration of

Policy" that this committee and Congress provided in IGRA. In particular, IGRA's policy provision found that existing Federal law in 1988 did not provide clear standards or regulations for Indian gaming. 25 U.S.C. § 2701. To address this and other congressional concerns regarding tribal gaming and to protect such gaming as a means of generating revenue to promote tribal economic development, self-sufficiency, and strong tribal government, this committee and Congress went on to expressly declare in IGRA that it was necessary to establish both Federal standards and the NIGC as an independent Federal regulatory authority for Indian gaming. 25 U.S.C. § 2702. Needless to say, the Colorado River Indian Tribes decision has the potential to seriously compromise our ability to effectively regulate Indian gaming in the manner Congress expected and expressed in its "Declaration of Policy" in IGRA.

The NIGC considers the MICS to be one of the most effective regulatory tools available to protect Indian gaming. We appear before the Committee today to seek Congressional action clarifying the NIGC's authority to regulate Class III gaming generally, and to promulgate and enforce our MICS regulations for Class III gaming specifically. The NIGC has submitted to Congress on March 23, 2005, a draft bill that, among other things, would amend IGRA to clarify the NIGC's authority to regulate Class III gaming generally, and to promulgate and enforce its MICS regulations for Class III gaming specifically. Although the NIGC and the Department of Justice are considering an appeal in this case, we believe the best way to resolve this question and prevent a potentially serious lapse in regulatory authority created by this court decision is by way of a legislative fix--language that makes absolutely clear the NIGC's authority with respect to Class III gaming.

In this connection, let me be crystal-clear. We are not asking Congress to expand the role NIGC has played in the past regarding Class III gaming. We merely ask that the law be clarified so that we may continue what has proved to be a very successful coordination of tribal, state and federal participation in the oversight of Class III gaming. This gaming produces four-fifths of overall tribal gaming revenue.

I. A HISTORY AND EXPLANATION OF MINIMUM INTERNAL CONTROL STANDARDS

In the years since the Indian Gaming Regulatory Act (IGRA), 25 U.S.C. § 2701 *et seq.*, was passed, Indian gaming has grown exponentially from $100 million in revenue to over $19.4 billion in 2004. Approximately 80% of this revenue comes from the higher stakes Class III gaming. Revenues from Indian gaming have built roads, schools and health centers on reservations across the country, and greatly reduced reservation unemployment in many areas.

As knowledge and expertise of gaming regulation grew, tribes recognized the need for internal controls. The National Indian Gaming Association (NIGA) and the National Congress of American Indians formed a task force which evaluated the minimum internal control standards of established gaming jurisdictions such as Nevada and New Jersey. The task force then created a set of internal control standards which tribes could choose to adopt. These standards became known as the "NIGA MICS."

Throughout the country, tribal gaming operations and tribal gaming commissions benefited from this effort, but it was a voluntary arrangement. Many tribes either did not adopt or enact the NIGA MICS or equivalent internal controls, or if they did, did not require strict adherence to them.

Of course, even before the NIGA MICS, there were a number of tribal gaming operations that had utilized and enforced very sophisticated minimum internal control standards which likely were more stringent than and exceeded those promulgated by the associations. However, as the NIGC monitored tribal gaming operations and observed the imposition of standards by states and tribes, it became apparent that, for many tribes, actual operation did not always comport with the internal control standards adopted by the tribe. The NIGC noted there were a number of places in Indian country where not only were these standards not being met, but such good practices were plainly ignored.

In addition, even for the tribes gaming pursuant to tribal-state compacts, the NIGC observed that details of the operations of tribal gaming and its regulation was often absent from the negotiated compacts; that in many instances the states' assigned role was minimal; and that in even more instances the actual participation of the states in regulatory oversight of tribal gaming operations was even less significant. This is not to say that an arrangement whereby a tribe has the sole responsibility for the regulation of its own gaming is unworkable. However, when no other entity has any significant oversight role, there develops the perception that the fox is watching the hen house. This perception can lead to a public distrust of the integrity of Indian gaming. In every other gaming jurisdiction, there is an oversight role for an entity that is separate from management of the gaming, and we believe that is what was intended and required under IGRA, and what has worked remarkably well since the implementation of the NIGC MICS. It is human nature to tend to do a better job when one knows that independent eyes occasionally fall on one's work. This is true in Indian gaming as well.

In response to its observations, the NIGC embarked on an effort to promulgate a comprehensive set of internal control standards for tribal gaming operations in accordance with accepted gaming industry good practices and pursuant to the authority vested in the Commission by the IGRA. In close consultation with tribes and with the assistance of a Tribal Advisory Committee, in 1999 the NIGC promulgated the MICS.

The MICS provide a comprehensive system of checks and balances to ensure control of all gaming revenues and gaming resources. The MICS are detailed internal procedures that tribes must meet both for the games offered for play and for support activities of the gaming. The internal controls thus cover cash handling and counting; internal audits; camera surveillance; the offering of credit; and information technology as well as the games themselves. They offer uniformity and consistency on an industry-wide basis while allowing variances to meet the specific needs of each tribe. In this way, the MICS protect the integrity of the gaming operation and ensure that gaming revenue is not lost through theft or embezzlement.

Many tribes have adopted NIGC's MICS verbatim and others have adopted even more stringent standards. However, while development and adoption of these standards is vital to protecting the assets of a gaming operation, MICS are only truly effective if the employees and management of a gaming operation properly implement and consistently follow them. Therefore, it is necessary for each tribal gaming operation to have proper auditing procedures as this ensures that the internal controls are properly implemented and allows the tribe to discover methods of improving them. In addition to the internal audit requirements, the NIGC also conducts periodic "MICS compliance audits" of Indian gaming operations. The MICS audit ensures that the tribe has developed internal controls at least as

stringent as the NIGC's MICS, and that the gaming operation complies with them. Exceptions are noted and communicated to both management and the tribe. A subsequent visit to the audited gaming facility is then scheduled, and the NIGC returns to verify that the requested corrections were made. In most cases, both the NIGC and tribe are pleased with the progress made because of the improved protection for tribal gaming revenues and assets.

Recent NIGC MICS audits have revealed significant internal control weaknesses at a number of tribal casinos. At a facility in the Great Plains, we discovered that the tribe was not performing statistical analysis of actual to expected results; that access keys and information technology were not adequately protected; and that the people handling the money were accountable only to themselves. Another facility in the Southern Plains had failed to segregate duties such that the same individuals were both counting funds removed from the gaming machines and maintaining the accountability and physical possession of these funds. This serious lapse in security of the tribal gaming revenues was compounded by the lack of an internal audit system. At some operations we have discovered so many internal control deficiencies that we have convinced the tribes to voluntarily close the facilities until the problems can be corrected. In other instances we are prepared to close facilities without the tribe's cooperation due to the seriousness of the situation.

The closing of a tribal gaming facility is, fortunately, a final option we have had to invoke only rarely. We always begin by working with the tribe to correct the weaknesses found, usually with great success. NIGC auditors found problems at a facility in the Southwest that included an ineffective internal audit department, surveillance problems, lack of statistical game analysis, and missing documentation for cashier cage

accountability. This tribe submitted a plan outlining how it intended to fix the deficiencies within a six month period and the NIGC confirmed through follow-up testing that the tribe had successfully remedied the deficiencies in its internal controls. Similarly, the NIGC and a tribe in the West used the same method to remedy NIGC audit findings that included surveillance problems; computer network security lapses; cashier cage documentation lacking employee signatures and independent verification of transactions; and soft count sheets filled out and signed prior to the count of funds. Comparable success stories exist throughout the nation which illustrate the extent to which the NIGC MICS regulatory program has benefited tribal gaming.

II. THE CRIT DECISION AND ITS THREAT TO THE EFFECTIVE REGULATION OF CLASS III GAMING

The reason I am here today is that a tribe engaged in class III gaming pursuant to a compact challenged the NIGC's regulatory authority to impose the MICS on Class III gaming operations and received a district court decision in its favor.

The CRIT decision resulted from an appeal of an NIGC Final Commission Decision and Order, issued in July 2003, which concluded that the Colorado River Indian Tribes (Tribe or CRIT) violated NIGC regulations when it denied Commission representatives access to the Tribe's gaming facility to conduct a MICS audit of the Tribe's Class III gaming activities. The Tribe filed suit in D.C. District Court in January of 2004, alleging that the NIGC exceeded its statutory authority under the IGRA. Recently, on August 24, 2005, the District Court issued an order finding that the NIGC exceeded its statutory powers in promulgating and enforcing the MICS for Class III gaming. In issuing its decision, the Court reviewed the text, structure, purpose, and legislative history of the IGRA.

Despite our belief that the MICS are fundamental to the integrity of Indian gaming, tribes have long questioned our authority to regulate the Class III gaming that accounts for most of the revenue in the industry. As the NIGC continues to attempt to enforce Class III MICS on all but the CRIT Tribe, it will face the threat of multiple lawsuits. The NIGC has many ongoing MICS compliance efforts that are already hindered by the threat of litigation. For instance, there are at present fourteen (14) ongoing NIGC MICS compliance audits that are at various stages of completion. The gaming operations in question range from an operation conducting less than $5 million in gross gaming revenue to one producing over a billion dollars in gross gaming revenue. Several of the tribes in question have already expressed their position that, because of the District Court's opinion, completed audits are now moot and those tribes do not need to remedy any noncompliance with Class III MICS. Also, several other tribes are questioning the NIGC's authority to conduct MICS audits at their operations. Yet other tribes have already indicated their intent to forego some MICS requirements, such as the independent annual audit of internal controls.

The District Court opinion addressed only our authority with respect to Class III gaming, not Class II gaming. However, the MICS are not class specific, and from a practical standpoint it is impossible to separate Class II from Class III revenues for the entire movement of money through the gaming operation. The MICS dictate procedures, not only for each game, but for cash handling, surveillance, and accounting. Most tribal gaming operations offer both Class II and Class III games in their facilities. Once the revenues have been collected from each game, they are necessarily commingled. It is not possible or practical to segregate and maintain Class II gaming revenues separately. Thus,

because the MICS relating to cash handling and accounting would necessarily infringe on the Class III activities of the gaming operation, strict adherence to the District Court decision could force a total removal of the MICS from most gaming operations.

Although the IGRA is replete with examples of NIGC's clear statutory authority over Class III gaming, the District Court interpreted other sections of IGRA to mean that Class II gaming is to be regulated by tribes and the NIGC and that Class III gaming is to be regulated solely by tribes and states. Even if this were a proper interpretation, however, the reality is that, by and large, states have not taken an active role in the regulation of Indian gaming.

As illustrated by the chart attached to my written testimony, there are twenty-two (22) states that have entered into compacts with tribes for Class III gaming. Of these compacts, four (4) do not address internal control requirements at all. Six (6) of them require very limited controls, such as the display of rules of play, maintenance of lists of barred persons, or minimal surveillance. A compact in one (1) state provides for tribal internal controls reviewed by that state, and in one (1) other state, compacts specify different levels of internal controls. Compacts in two (2) states require the adoption of state standards or their equivalent, and compacts in four (4) states set forth thorough, comprehensive internal controls. Additionally, in several states, the compact terms detailing casino controls would be eviscerated without the NIGC's MICS: compacts in four (4) states expressly adopt the NIGC MICS or standards at least as stringent. From this review it is evident that many compacts have internal control provisions not up to the standards required by the NIGC MICS or states such as New Jersey or Nevada. As is clear from the chart, strict application of the District Court decision would remove

internal control requirements, where a party independent from the ownership and management of the tribal gaming plays a role, in several states.

Further, even when compacts contain adequate internal control provisions, not all states make enforcement of violations a priority. In fact, there are several states with compacts that take no appreciable role in the regulation of Class III tribal gaming within their borders. Thus, without NIGC MICS and their supporting audits, there will effectively be no oversight regulation in those states.

Some tribes have asserted that the NIGC's authority to promulgate and monitor compliance with standards for Class III gaming intrudes upon tribal sovereignty. The Act recognizes and balances Tribal, Federal, and State interests. The IGRA as written requires tribes to debate whether they wish to cede a small portion of their sovereignty in order to game and thereby increase tribal funding to carry out other sovereign tasks. If a tribe opts to invest in gaming it must protect itself and its assets. The Federal government also seeks to protect this investment in tribal sovereignty by ensuring tribal gaming succeeds, for a scandal at one gaming facility has the ability to negatively affect all operations. The vast majority of visitors to the gaming facilities are non-Indian and these visitors will only continue to patronize tribal gaming operations if the hard-won reputation for integrity and well-regulated gaming is maintained. The most effective measure of any nation's sovereignty is its ability to provide for its needs and the needs of its people. Self-sufficiency for tribal nations is a stated goal of the IGRA. Weakening the strong regulation of Class III gaming thus works against tribal sovereignty and self-sufficiency.

III. CONCLUSION

As I have previously noted, there is a long history of tribal challenges to our Class III authority. These challenges have prompted us to appear before this Committee in the past to ask for legislation clarifying our authority. Now that a court has spoken to the issue we must again, and with renewed vigor, ask this Committee to support legislation that eliminates any question regarding our legal authority to monitor and regulate Class III gaming and that clarifies that NIGC authority over Class III gaming is as broad as it is over Class II gaming.