

CALIFORNIA SETS STANDARDS FOR TRIBAL SUBSIDIARIES' SOVEREIGN IMMUNITY

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California Sets Standards for Tribal Subsidiaries' Sovereign Immunity

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In a major sovereign immunity decision issued December 22 in *People v. Miami Nation Enterprises*, (Cal. 2016) ("MNE"), the California Supreme Court (1) clarified the burden of proof that applies when a tribal corporation asserts sovereign immunity, (2) identified five factors that should be considered to determine whether an entity is an "arm of the tribe" entitled to share the tribe's immunity and (3) explained how lower courts should apply those factors. Tribal corporations will find it more difficult to assert sovereign immunity in California as a result of the Court's decision.

The Commissioner of the California Department of Corporations had sued "payday loan" businesses owned by Miami Nation Enterprises (MNE), the economic development authority of the Miami Tribe of Oklahoma, and SFS, Inc., a corporation wholly owned by the Santee Sioux Nation. The trial court dismissed, holding that the two tribal entities and their cash-advance and short-term-loan businesses were "arms" of the tribes entitled to share their sovereign immunity. The appellate court affirmed but the California Supreme Court reversed, holding that, on the record before the court, neither of the tribal defendants had shown that it was entitled to sovereign immunity. The Court remanded to the trial court to determine whether additional litigation of the issue was warranted.

Procedurally, the Court held that a tribal entity asserting immunity bears the burden of proving, by a preponderance of the evidence, that it is an "arm of the tribe" entitled to tribal immunity. This will make it more difficult for tribal entities in California to get lawsuits dismissed by filing affidavits from corporate officials. Courts are likely to permit plaintiffs to conduct discovery to look behind the affidavits to determine whether the entity is entitled to immunity under the test prescribed by the Court.

Substantively, the Court identified five factors that determine whether an entity is an “arm” of its tribal owner: (1) the entity’s method of creation, (2) whether the tribe intended the entity to share in its immunity, (3) the entity’s purpose, (4) the tribe’s control over the entity, and (5) the financial relationship between the tribe and the entity. While other courts, including the Ninth and Tenth Federal Circuit Courts of Appeals, have adopted similar tests, the *MNE* decision is significant because of the priority it gives the “functional” over the “formal” factors:

1. With respect to method of creation, the Court adopts the widely shared view that “[f]ormation under tribal law weighs in favor of immunity... whereas formation under state law has been held to weigh against immunity ... or to constitute a waiver of immunity.” The Court’s comment that the “circumstances under which the entity’s formation occurred, including whether the tribe initiated or simply absorbed an operational commercial enterprise, are also relevant” means tribal acquisition will not necessarily transform an existing company into an immune entity.
2. With respect to the tribe’s intent, the Court commented that “this factor will generally weigh against immunity if the record is silent as to the tribe’s intent” while minimizing the importance of intent when it does appear in the record: “[T]ribal intent, as expressed in the entities’ articles of incorporation, reveals little about whether the entity acts as an arm of the tribe so that its activities are properly deemed to be those of the tribe. ... The Tribes’ self-interested and unsupported claim that they intended their sovereign immunity to extend to SFS and MNE Services cannot, without more, support immunity”
3. With respect to the entity’s purpose, formal declarations help but are insufficient unless reflected in economic reality: “If the entity was created to develop the tribe’s economy, fund its governmental services, or promote cultural autonomy, its purpose pertains to tribal self-governance notwithstanding the entity’s commercial activities. ... If the entity’s stated purpose is sufficiently related to tribal self-governance, the inquiry then

examines the extent to which the entity actually serves that purpose. ... An entity whose declared purpose is to further the tribe's economic development may bolster its case for immunity by proving, for example, the number of jobs it creates for tribal members or the amount of revenue it generates for the tribe. By contrast, evidence that the entity engages in activities unrelated to its stated goals or that the entity actually operates to enrich primarily persons outside of the tribe or only a handful of tribal leaders weighs against finding that the entity is an arm of the tribe."

4. With respect to control, the Court does not, as some other courts have done, prescribe the number of board members that must be tribal members or the powers that elected officials must retain. The Court does, however, require evidence of active oversight: "An entity's decision to outsource management to a nontribal third party is not enough, standing alone, to tilt this factor against immunity" but "[e]vidence that the tribe actively directs or oversees the operation of the entity weighs in favor of immunity; evidence that the tribe is a passive owner, neglects its governance roles, or otherwise exercises little or no control or oversight weighs against immunity."
5. Finally, with respect to financial relationship: "If a significant percentage of the entity's revenue flows to the tribe, or if a judgment against the entity would significantly affect the tribal treasury, this factor will weigh in favor of immunity even if the entity's liability is formally limited. ... Determining whether this factor weighs in favor of immunity requires a consideration of degree rather than a binary decision. But because any imposition of liability on a tribally affiliated entity could theoretically impact tribal finances, the entity must do more than simply assert that it generates some revenue for the tribe in order to tilt this factor in favor of immunity."

By unilateral action, a tribe can form an entity under tribal law and include in the articles and bylaws expressions of the tribe's intent that the entity be immune from suit and provisions that its purpose is to provide revenue to

fund housing, health and other tribal governmental needs. While failure to take these actions will likely weigh *against* immunity, taking them will not assure the entity's immunity. Under the *MNE* decision, California courts will focus instead on the number of jobs provided for tribal members, the degree of oversight that the Tribe exercises over the entity, the amount of money flowing from the entity to the tribe and the significance of the revenues to the tribe.

California is home to over 100 tribes. The decision in *MNE* will directly impact those tribes and, in addition, likely influence other courts.

Godfrey & Kahn works with tribes on labor and employment law issues of every sort, including union organizing, EEOC claims, Fair Labor Standards Act, tribal preference, insurance, development of tribal employment laws, employee handbooks, etc. For more information, contact Brian Pierson at 414.287.9456 or bperson@gklaw.com.

