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On Indian Casino Compacts

By

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As the State of Florida negotiates a compact with the Indian tribes regarding the taxation of tribal casinos, it should avoid the mistakes of other states, most of which have left billions of dollars on the table through poorly designed compacts that were highly favorable to Indian tribes.

Indian gaming is a sizeable business in Florida, and revenues for 2006 were \$1.6 billion, according to the Indian Gaming Industry Report. Based on the tribes' near-monopoly position and their exemption from federal, state and local taxes, their casinos are extremely profitable. The tribes do not report financial results publicly, but a reasonable estimate of operating income before third-party management fees, interest payments and rental expenses is \$1 billion annually. Indeed, if the tribal casinos were listed on the New York Stock Exchange, the resulting shares would have a market value in the billions.

It is clear that the tribes can afford to pay substantial taxes to the state, and the question becomes the following: how much is appropriate? The new racetrack slots operators in Broward County pay a 53% gaming tax, which includes state and local levies. If mandatory allocations to track purses are counted as a tax, the effective rate increases several percentage points. With these tax rates, the non-Indian operators expect to be profitable, and they have sunk hundreds of millions of dollars into constructing slots parlors and associated amenities.

A percentage tax rate in the mid 50s is thus a logical starting point for the State of Florida in proposing a fair tax rate on Indian gaming revenues. From this figure, the tribes can reasonably

argue for deductions that are required to maintain profitability in light of the terms of existing management and financial contracts, all of which were signed by the tribes pre-compact. A sensible compromise is likely to be a 40% tax rate, which will insure the tribal casinos' ongoing prosperity.

Despite Indian casinos' monopoly status in many jurisdictions, the highest Indian gaming tax is currently 25%, and most states fail to achieve even this modest goal. Problems arise from the states' lack of knowledge regarding casino economics, their reliance on gaming lobbyists for basic information (as opposed to independent experts), the influence of tribal political donations on the negotiating process, and the misguided perception that a 25% rate is a federally mandated ceiling.

Florida must try and avoid these problems in its new compacts. In exchange for a fair tax, the state can offer the tribes Class III "Las Vegas style" slot machines instead of the Class II "bingo style" machines now in use. This concession alone should increase slots revenues by 20%. Allowing a greater variety of table games in the casinos would boost revenues another 15%. If the tribes refuse to negotiate in good faith and seek a better deal from the federal agency that set the 60-day deadline, the state should consider legalizing casinos that compete directly with the tribal facilities. Having a new competitor across the street will damage a tribal casino's fortunes more than any state-mandated tax.

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