

Tribal Sales on the Hot Seat

There's been a noticeable increase in the struggle for control of the regulatory landscape involving the states and those parties selling cigarettes on tribal land; not surprisingly the trend is towards additional regulation and increased revenues for states. >BY THE TOBACCO TEAM

NEW TRIBAL CERTIFICATION RULES

In the area of tribal sales of cigarettes produced by non-participating manufacturers, several states now take the position that a brand meant only for tribal sale and not stamped with a state excise tax stamp must be "certified" and included on the state's Tobacco Directory prior to making any sales on tribal land. This trend changes drastically from prior practice under which it was generally accepted that no certification was required for sales on tribal lands. These states also contend that there can be no shipment of any cigarettes into the state, stamped or not, that do not appear on their Tobacco Directory and that penalties of up to 500% of the retail value of cigarettes can result. This affects any transport of cigarettes to or from tribal lands within or between one of these states, thereby increasing the number of manufacturers and brands that are required to be certified.

WHEN ARE CIGARETTES SOLD?

When cigarettes are manufactured on tribal land and then sold tribally, generally the manufacturer and the purchaser assert that such cigarettes were "not intended for distribution or sale in the State" and were "only intended for distribution or sale tribally." Assuming the assertion is true, as a matter of law in most states, such cigarettes should not be considered as being "sold" within that State, given that they are cigarettes transported between two sovereign nations.

Most state tobacco laws define the term "units sold" to mean "the number of individual cigarettes sold in the state by the applicable tobacco product manufacturer (whether directly or through a distributor, retailer, or similar intermediaries), as measured by excise taxes collected by the state on packs (or 'roll-your-own' tobacco containers). Therefore, to be counted as being a "unit sold" in most

states, individual cigarette packs must bear a state excise tax stamp. Because cigarettes sold on Native American lands in most states are not required to bear any excise stamp, they cannot—and should not—be counted as "units sold." When no state excise tax stamp is affixed or intended to be affixed to a tribally-sold cigarette, arguably these cigarettes cannot be considered to be "sold" for purposes of escrow obligations or any related statutes.

NY: NO RESALE OF UNSTAMPED CIGS

On December 15, 2008, New York Governor David Paterson signed into effect a new law requiring stamping agents in New York to sign an affidavit under penalty of perjury saying that they will not resell unstamped cigarettes in violation of Article 20 of the state's tax law—the section that deals with cigarette taxes. The law aims to curb Indian reservation stores from selling untaxed cigarettes to non-Indians by requiring suppliers to have state tax stamps. New York has claimed that it has lost hundreds of millions of dollars annually in tax revenue due to sales of untaxed cigarettes sold tribally. The practical effect could be that many tribal sales could now be subject to escrow, as well, given that cigarettes become subject to an escrow obligation when packs are stamped and that applicable state excise tax is paid. The State has recognized, however, that sales to Indians must remain untaxed.

Tribal leaders have rightfully rejected the role of the state tax collector, maintaining that sovereignty and treaty rights exempt nations from any obligation to collect state taxes. The new requirements in New York have been temporarily put on hold as a result of a lawsuit filed soon after the law went into effect on behalf of a wholesaler and stamping agent as well as a member of the Seneca Nation of Indi-

ans who owns and operates wholesale and retail tobacco businesses licensed by the nation.

At a January hearing, the New York State Supreme Court extended, until December 24, 2009, a previously issued preliminary injunction that stops the State, and anyone charged with enforcing the State's tax laws, from restricting State stamping agents from selling unstamped cigarettes to reservation cigarette sellers, or restricting reservation retailers from selling unstamped cigarettes to tribal and non-tribal members until the state Department of Taxation and Finance develops a viable system to distribute tax-exempt coupons for sales to tribal members.

The New York law represents a growing trend of states that are looking in the direction of tribal smoke shops and other Native American cigarette outlets as potential sources of state revenue.

LITIGATION AGAINST SMOKE SHOPS

States have also expanded to suing smoke shops in addition to manufacturers and distributors. For instance, Oklahoma recently filed a lawsuit against fourteen individuals who own or operate Creek Nation-affiliated smoke shops, alleging they conspired to make unlawful profits by selling cigarettes without proper tax stamps and without certification on the State's Tobacco Directory, all in violation of the Federal Contraband Cigarette Trafficking Act, State Complementary Act, and State Cigarette Tax Act.

This lawsuit appears to be more tangible evidence of the shifting regulatory and litigation landscape. Most observers and practitioners believe that the budgetary pressures created by the current economic crisis and decrease to the states of U.S. dollars will result in even more regulatory activity designed to increase the amount of revenue collected by the states. ■

The Tobacco Team at Richmond, Va.-based Troutman Sanders consists of partners, attorneys of counsel, and associates with experience and expertise in tobacco regulatory issues and litigation to represent the specialized needs of tobacco product manufacturers, importers, distributors, and retailers. Visit: www.troutmansanders.com/tobacco/