

ONLINE SOVEREIGNTY: THE LAW AND ECONOMICS OF  
TRIBAL ELECTRONIC COMMERCE

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Introduction .....	1
I. The Law and Regulation of Online Tribal Lending .....	6
A. Tribal Governments and CRA .....	7
B. Tribal Government Inclusion in the Dodd-Frank Act .....	8
C. TLEs Improve Access to Mainstream Financial Institutions .....	10
D. The Indian Gaming Regulatory Act as an Analogue .....	11
E. An Indigenous Rights Perspective.....	13
II. Economic Impact of Tribal Online Lending .....	13
A. Lac Vieux Desert Band of Lake Superior Chippewa.....	13
B. Otoe-Missouria Tribe .....	14
C. Habematolel Pomo of Upper Lake Tribe .....	15
D. Other Tribal Lenders .....	17
III. The Problem with Outside Regulation .....	18
A. State Assaults on Tribal Sovereignty .....	19
B. Tribal Consumer Protection Best Practices.....	21
C. State and Federal Assaults on Tribal E-Commerce .....	25
Conclusion .....	26

INTRODUCTION

In an 1886 case the US Supreme Court wrote that for Indian tribes “the people of the states where they are found are often their deadliest enemies.”<sup>1</sup> Although that observation is nearly 150 years old, and reasonable neighborliness has developed in most instances between tribal governments and their surrounding communities, certain state agencies and regulators have continued that tradition of hostility in terms of tribal economic development prospects, particularly in the arena of electronic commerce or “e-commerce.”

Numerous states have recently attempted to regulate businesses operated by tribal governments that are more properly subject to regulations established by tribal law and subject to federal oversight. Despite the fact that these businesses operate exclusively under tribal law and make their tribal affiliation clear to customers, certain state regulators have demanded absolute compliance with state

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<sup>1</sup> *US v. Kagama*, 118 US 375

law, even when such laws are from states thousands of miles away. Not only does this overreaching by uninformed state regulators limit the products available to consumers but it also severely undercuts on-reservation economic development and challenges basic notions of tribal sovereignty.

On-reservation tribal businesses are vital to the sovereignty and welfare of tribal governments and American Indians/Alaska Natives nationwide. In 2014 the US Supreme Court reiterated that, “(a) key goal of the Federal Government is to render Tribes more self-sufficient and better positioned to fund their own sovereign functions, rather than relying on Federal funding.”<sup>2</sup> With dwindling federal funds, tribal communities face significant challenges in establishing steady revenue streams and attracting external investors.<sup>3</sup> While not exclusively linked to location, these challenges to tribal economic development are often entrenched because a majority of reservation lands are geographically isolated, historically disadvantaged, and poor.

The vast majority of tribal communities struggle with long-standing cycles of poverty, and as with other developing nations, the need for economic development on tribal lands remains acute and affects nearly every aspect of reservation life. Large portions of Indian Country lack basic infrastructure, posing a daunting barrier to tribal leaders’ attempts to develop their economies. Such realities highlight the importance of stimulating economic development for tribal community social and economic recovery. Research from the 2006-2010 American Indian Community Surveys indicates that the pace of reservation economic growth slowed between 2000 and 2010. While economic growth on reservations outpaced the United States during the recession, the income gap between reservations and the rest of the United States remains large, with the real per capita income for American Indians on reservations at \$10,963 compared to \$26,648 for US all races. Economists now speculate that current growth rates on reservations have slowed the pace for closing the gap until at least the year 2080.<sup>4</sup>

Although tribal leaders have acknowledged and attempted to reduce these problems for decades, they have not had the resources to create a more hospitable business environment. A vicious cycle has consequently developed: businesses avoid establishing a presence on reservations because of the lack of infrastructure, while tribal governments are left unable to improve their infrastructure because on-reservation commerce is woefully insufficient.

In an effort to break this cycle and raise critical governmental revenues, tribal leaders have relied on their most tangible sustainable competitive advantage: their tribal sovereignty. As nations that predate the Constitution and the United States, tribal nations can generally operate in licensed environments independent of state

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<sup>2</sup> *Michigan vs. Bay Mills Indian Community*, 134 S. Ct. 2024, 2043 (2014) (Sotomayor, J. concurring)

<sup>3</sup> Cornell and Kalt, *Sovereignty and Nation-Building: The Development Challenge in Indian Country Today*. Harvard Project on American Indian Economic Development, available at [www.ksg.harvard.edu/hpaied](http://www.ksg.harvard.edu/hpaied)

<sup>4</sup> Randall K.Q. Akee & Jonathan B. Taylor. (2014). *Social and Economic Change on American Indian Reservations: A Databook of the US Censuses and the American Community Survey 1990 – 2010*, available at <http://taylorpolicy.com/us-databook/>

regulation. This notion of excluding state law and regulatory authority is one of the founding principles of the Supreme Court's Indian Law jurisprudence and stems from an 1832 case, *Worcester v. Georgia*.<sup>5</sup> In that case, the state of Georgia passed a law requiring any non-Native person living within the borders of the Cherokee Nation to get a license to do so from the state. Several missionaries, including Rev. Worcester, defied the law, were arrested, and sentenced to four years of hard labor. On appeal to the Supreme Court, the Justices found that the Cherokee Nation was, "a distinct community, occupying its own territory, with boundaries accurately described, in which the laws of Georgia can have no force."

As the Chairwoman of the Habematolel Pomo Indians of Upper Lake recently testified before the House Committee on Financial services,

The inherent sovereign power of Indian Tribes predates the United States Constitution. Indian Nations appears twice in the Constitution, each time in Article I, treated as separate and existing sovereign nations. Nearly every piece of modern legislation dealing with Indian tribes explicitly affirms the protective trust relationship between tribes and the federal government. The federal trust responsibility to Indian tribes underlies both the "government-to-government relationship" with Indian tribes and the imperative that federal agencies not actively impede the economic development and self-determination of Indian tribes, and that they engage in meaningful consultation when any federal undertaking might impact tribes in a significant way. The sole power to diminish tribal sovereignty rests with Congress. Whatever Congress has not expressly diminished by legislation remains for the exercise of tribal governments.<sup>6</sup>

By leveraging this sovereignty to their advantage<sup>7</sup>, some tribal governments have relied on gaming and a lack of sales tax to entice consumers to visit and invest in their communities. Contrary to popular belief, however, gaming does not provide a sufficient economic or social recovery for most tribal economies. A majority of the more than 560 federally-recognized Indian tribes do not have any significant gaming operations,<sup>8</sup> and of those that do, only a small handful generate

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<sup>5</sup> 31 U.S. 515 (1832)

<sup>6</sup> Testimony of Chairwoman Sherry Treppa, Habematolel Pomo of Upper Lake, before the United States House of Representatives Committee on Financial Services, "Short-Term, Small Dollar Lending: The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty," February 10, 2016, available at <http://financialservices.house.gov/uploadedfiles/hhrg-114-ba15-wstate-streppa-20160211.pdf>

<sup>7</sup> See generally Gavin Clarkson and James K. Sebenius, *Leveraging Tribal Sovereignty for Economic Opportunity: A Strategic Negotiations Perspective* 76 MISSOURI L. REV. 1045 (2011)

<sup>8</sup> Spilde, K., & Taylor, J. B. (2013). Economic Evidence on the Effects of the Indian Gaming Regulatory Act on Indians and Non-Indians. *UNLV Gaming Research & Review*

substantial revenues.<sup>9</sup> While a few tribes near major metropolitan centers operate successful gaming enterprises, hundreds of tribes have no gaming industry, and many operate small casinos located far from population centers.<sup>10</sup> Thus, the economic benefits of gaming are not universally distributed throughout Indian Country. For example, the unemployment rate still hovers around 50% for Indians who live on reservations, nearly ten times that for the US as a whole,<sup>11</sup> and more than one third of American Indian children live in poverty.<sup>12</sup>

The dawn of the Internet Age, however, ushered in a variety of new opportunities for tribes located in rural locations that became hotbeds for business innovation. Most significantly, tribal governments realized that they could export services via the Internet to transact business with consumers anywhere in the country while still being subject to tribal law alone. The key to this arrangement was conducting business so that all transactions occurred on the reservation and ensuring that consumers consented to the application of tribal law instead of state law. Seizing upon this model, tribal governments began offering small-dollar loans to consumers who needed money quickly or were unable to obtain funding from traditional sources. Customer need and response to these financial services was overwhelming, and much-needed government revenues began to flow into some of the most needy tribal communities.

The tribal-owned businesses that made these loans were organized to take advantage of the sovereign authority that their tribes exercised over the reservation. Under this arrangement, consumers flocked to tribal lenders and exemplified a classic *quid pro quo*. Tribal businesses provided consumers with small-dollar loans

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*Journal*, 17(1). According to the National Indian Gaming Association, only 224 tribes have gaming operations of any kind as of 2005. NAT'L INDIAN GAMING ASS'N, AN ANALYSIS OF THE ECONOMIC IMPACT OF INDIAN GAMING IN 2005 2 (2005), available at [http://www.indiangaming.org/NIGA\\_econ\\_impact\\_2005.pdf](http://www.indiangaming.org/NIGA_econ_impact_2005.pdf).

<sup>9</sup> See NAT'L GAMBLING IMPACT STUDY COMM'N, NATIONAL GAMBLING IMPACT STUDY COMMISSION REPORT, at 2-10 (1999), available at <http://govinfo.library.unt.edu/ngisc/reports/2.pdf> ("The 20 largest Indian gambling facilities account for 50.5% of total revenues, with the next 85 accounting for [only] 41.2%. Additionally, not all gambling facilities are successful. Some tribes operate their casinos at a loss and a few have even been forced to close money-losing facilities."). Note also that many tribes that do generate significant revenues often must share those revenues with the state as part of the compacting process of the Indian Gaming Regulatory Act. See 25 U.S.C. §§ 2701–2721 (2006). In some cases, such as with the Mohegan and Mashantucket Pequot tribes in Connecticut, the revenue share is as high as 25%. See e.g. Gavin Clarkson and Jim Sebenius, Leveraging Tribal Sovereignty for Economic Opportunity: A Strategic Negotiations Perspective, *Missouri Law Review* (2012)

<sup>10</sup> See Donald L. Barlett & James B. Steele, *Wheel of Misfortune*, *TIME*, Dec. 16, 2002, at 44.

<sup>11</sup> See Bureau of Indian Affairs, *2005 American Indian Population and Labor Force Report*, available at <http://www.bia.gov/cs/groups/public/documents/text/idc-001719.pdf>

<sup>12</sup> See, e.g., NAT'L CTR. FOR EDUC. STATISTICS, U.S. DEP'T OF EDUC., AMERICAN INDIAN AND ALASKA NATIVE CHILDREN: FINDINGS FROM THE BASE YEAR OF THE EARLY CHILDHOOD LONGITUDINAL STUDY, BIRTH COHORT (ECLS-B) 3 (2005), available at <http://nces.ed.gov/pubs2005/2005116.pdf>.

that other lenders were unwilling or unable to offer, and in return, consumers agreed to enter into loan agreements consummated on tribal land that were subject only to tribal law. Believing this arrangement to be a reasonable transaction, thousands of customers obtained much-needed funds on short notice from tribal lenders via the Internet. Many of them became repeat customers who, despite being offered multiple alternatives off-reservation (both online and from land-based operations) intentionally chose to return virtually to the reservation to obtain additional financing.

State efforts to regulate or even prohibit tribal-regulated lending began just as the model was being streamlined and perfected. Even though consumers explicitly agreed that their loans were subject only to tribal laws, states began suing tribal lenders for failing to obey local lending laws and failing to obtain state certifications. Initial tribal objections to these regulations relied upon the fact that the prevailing federal legislation, the Dodd-Frank Act,<sup>13</sup> acknowledged that tribes are to be treated as states for the purposes of financial services. In spite of a clear federal mandate, attempted state regulation became more fervent and widespread. Faced with costly litigation in multiple states, many tribal government lenders were forced to cease or significantly reduce their operations, thereby cutting off the economic lifelines they had become in their communities. While it is unclear how this controversy will ultimately play out, one thing is certain: states are not only undermining tribal innovation and harming tribal economies but also attacking tribal sovereignty itself.

Businesses and consumers entering into commercial contracts rely heavily on consistency and predictability in contracting, including when the parties mutually agree to apply tribal law or utilize tribal courts to resolve disputes. Uniform interpretation and enforcement of such agreements are critical to ensuring continued investment in tribal businesses. With over one quarter of American Indians living in poverty, nearly twice the national average,<sup>14</sup> it has never been more important to promote confidence in the Indian economy. When courts do not give full force and effect to contracting parties' desire to resolve their private disputes using tribal courts and tribal law, this confidence is threatened.

Perhaps lost in the legal rancor, however, are the very real human and economic consequences of the loss of tribal lending as an e-commerce business, as well as the potential damage to tribal e-commerce as a whole. In presenting the results of our empirical research into the economic impact of tribal online lending in Indian Country, we first frame the issue in Part I with a brief summary of the legal foundations for tribal e-commerce and tribal lending in particular. In Part II we present several case studies of tribes that have engaged in online lending, focusing on the direct economic impact to those tribal communities. Part III concludes with policy arguments as to why state and federal regulators should support rather than suppress tribal e-commerce, including tribal small-dollar online lending.

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<sup>13</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub.L. 111-203) (2010)

<sup>14</sup> See U.S. Census Bureau, *Poverty Rates: 2007-2011*, available at <http://www.census.gov/prod/2013pubs/acsbr11-17.pdf>

## I. THE LAW AND REGULATION OF ONLINE TRIBAL LENDING

The market for small-dollar lending is broad and deep, and the conditions that support its growth pre-date tribal government involvement in the industry. Tribal small-dollar online lending would not exist without a market of “underbanked” consumers not adequately serviced by traditional lenders. The 2013 FDIC National Survey of Unbanked and Underbanked Households, define the underbanked as “those that have a checking or savings account but rely on alternative financial services such as check-cashing services, payday loans, rent-to-own agreements or pawn shops.”<sup>15</sup> According to that report, 9.6 million households representing 25 million people were unbanked in 2013. One in five (or 24 million households) were underbanked in 2013, consisting of an estimated 68 million people. More than a third (35.6 percent) of unbanked households reported the main reasons for not having an account being insufficient money to keep in an account or meet minimum balance requirements. In addition 34.1 percent of households that recently became unbanked experienced either a significant income loss or job loss that they said contributed to becoming underbanked. These consumers are not being served by traditional banks or lending institutions.

In spite of the federal government's attempt under the Community Reinvestment Act (“CRA”)<sup>16</sup> to incentivize banks to serve the communities they operate in, research reveals that the CRA operates inefficiently since the primary benchmark has been through bank regulator evaluations of individual banks performed about every two to four years. The CRA was intended to push banks to reinvest and has helped reign in “redlining” of poor communities, the long-time practice of not offering mortgages in “bad” neighborhoods. Though the Federal Reserve website invites comments because they and the other regulators are “currently considering what can be done to make CRA a more effective regulatory incentive going forward to address an unprecedented set of community needs,” the CRA has never even rated the availability of basic banking services for underserved consumers.

Given this lack of attention to underbanked Americans by the largest megabanks, tribal governments have stepped in to serve them remotely through online lending businesses located on tribal lands. While providing a critical service for financially fragile Americans, tribal governments are also able to better fulfill the mandate of the CRA since they actively invest the governmental revenues from their lending businesses into struggling tribal communities and surrounding regions and therefore relieve the social and economic burdens on and near tribal lands.

In many respects, tribal online lenders are responding not only to the vast unmet need but also to Congressional intent as embodied in the CRA.

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<sup>15</sup> 2013 FDIC National Survey of Unbanked and Underbanked Households. Available at <https://www.fdic.gov/news/news/press/2014/pr14091.html>.

<sup>16</sup> Community Reinvestment Act, *hereinafter* “CRA,” (P.L. 95-128, 91 Stat. 1147, title VIII of the Housing and Community Development Act of 1977, 12 U.S.C. § 2901 *et seq.*)

### A. Tribal Governments and CRA

Academic research in law and geography has revealed numerous ways that laws are intended to influence or control behaviors across physical space. A so-called “law and geography” analysis uses geographic tools to understand the consequences of legal policies and institutions, and scholars have addressed legal issues in a variety of areas. For example, several authors have used geographic analyses of mortgage lending patterns to demonstrate racial bias in the approval of credit applications. Previous geographic evidence was also used to demonstrate that storefront payday lenders disproportionately located their branches around military bases, persuading Congress to adopt a federal usury law and arbitration ban on some loans to military personnel.<sup>17</sup>

Geographic analysis also helped convince Congress that in some communities, banks accepted deposits but did not give out an equivalent amount in loans—a process called “disinvestment.” Accordingly, Congress adopted the CRA requiring that depository institutions make efforts to lend in low-and moderate-income neighborhoods within the contiguous geographic area surrounding their office or group of offices. In spite of the CRA requirements, however, New York City's Association for Neighborhood and Housing Development (“ANHD”) studies how the federal government's attempt under the CRA to make banks serve the communities they operate in actually affects low-income neighborhoods in the city.

Banks are bringing in record earnings but ANHD finds their investment insufficient “to truly help meet the credit needs of low- and moderate-income New Yorkers.” They report the city's 23 largest banks have deposits in the city exceeding \$590 billion but lend or invest only 1.35% of it in a way that benefits low and moderate-income residents. Even with average re-investment of 1.35%, the study found several banks -- Bank of America, JPMorgan Chase, Sovereign, Apple Bank, Astoria, Emigrant, Ridgewood, Morgan Stanley, Deutsche Bank, and Bank of NY Mellon -- each reinvested less than 1% of their New York City deposits in New York City. JPMorgan reinvested just .36% of its more than \$256 billion in city deposits and Deutsche Bank just .35%.

The four biggest American megabanks -- JPMorgan Chase, Citibank, Bank of America, and Wells Fargo -- have over 61% of all New York City deposits according to ANHD. They also have about half of all city government deposits in their banks, amounting to over \$230 million. But those institutions are not looking for low-income city resident depositors. That kind of financial investment in underserved communities is absolutely vital to those neighborhoods and residents, but it might not be the most critical thing banks fail to provide. In the era of “too big to fail” megabanks merging and buying out smaller institutions, immense competition exists for wealth management services and private banking for multi-

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<sup>17</sup> Graves, S.M. and Peterson, C.L. 2008. *Usury Law and The Christian Right: Faith-Based Political Power and the Geography of American Payday Loan Regulation*. 57 Cath. U.L. Rev. 637.

millionaires, but interest diminishes for vital banking services for low-income and poor people.

Tribal government innovation in short-term online lending serves the financially fragile and those subprime borrowers that traditional banks and institutions typically shun. Efforts by federal or state regulators to “choke off” access to credit for under-banked people in this country revealed the protectionism afforded to mainstream financial institutions as well as the ways that nonprime consumers are overlooked or actively ignored.

#### *B. Tribal Government Inclusion in the Dodd-Frank Act*

Unlike tribal government gaming where tribal authority to offer gaming on their reservations had to be established through a series of court cases culminating in *California v. Cabazon* in 1987, tribes’ authority to offer and regulate financial services is already enshrined in federal law.

Title X of the Dodd-Frank Act,<sup>18</sup> the Consumer Financial Protection Act of 2010 (the “CFP Act”) created the Consumer Financial Protection Bureau (the “CFPB”) to ensure “that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive.” The CFPB has the power to promulgate rules to administer and carry out the purposes and objectives of the CFP Act and 18 existing federal consumer financial protection statutes, each, an “Enumerated Consumer Law.” It also has the power to regulate activities relating to consumer real estate lending activities, payday loans, private student loans, and any larger participant of consumer financial products or services.

Congress’s drafting of the Dodd-Frank Act reveals its intention to include tribes among the financial regulators, and not the regulated because only one mention of tribes occurs in the Dodd-Frank Act in the definition of “State.” The term “State” means any state, territory, or possession of the United States...or any federally recognized Indian tribe, as defined by the Secretary of the Interior under section 479a-1(a) of title 25. Accordingly, each time “State” appears in the Dodd-Frank Act, Congress intended these provisions to cover tribes and to treat tribes in an equivalent way to states. Treating tribes as states is consistent with the general federal policy of encouraging tribes to strengthen self-government and to assume control over their business and economic affairs.

All of the references to states throughout the CFP Act highlight the cooperation Congress envisioned between the federal government and states (and thus tribes). For example, the Dodd-Frank Act: (i) requires the CFPB to coordinate “fair lending efforts of the [CFPB] consistent with other Federal agencies and State regulators, as appropriate, to promote consistent, efficient, and effective enforcement of Federal fair lending laws,” (ii) gives states a significant role in collecting and tracking consumer complaints and (iii) requires that, “[i]n developing and implementing registration requirements [for covered persons],” the CFPB must “consult with State agencies regarding requirements or systems (including coordinated or combined systems for registration), where appropriate.”

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<sup>18</sup> *Supra* note \_\_



Further reinforcing the idea that Congress intended states (and thus tribes) to be co-regulators, the Dodd-Frank Act promotes enforcement of state consumer protection laws and state power to directly enforce state and federal law. For example the CFPB Act provides that, but for a few exceptions, it “may not be construed as annulling, altering, or affecting, or exempting any person subject to the provisions of this subchapter from complying with, the statutes, regulations, orders, or interpretations in any State, except to the extent that any such provision of law is inconsistent with the provisions of this title, and then only to the extent of the inconsistency.” The CFPB Act also provides that “[n]o provision of this title, except as is provided in section 1083, shall be construed as modifying, limiting, or superseding the operation of any provision of an enumerated consumer law that relates to the application of a law in effect in any State with respect to such Federal law.”

Taken together, the text of the Dodd-Frank Act demonstrates that Congress intended tribes to be the CFPB’s partners in financial services regulation, independent of state intervention. The Department of Treasury supported this suggestion when it stated that the Dodd-Frank Act “[e]mpower[s] tribal government...to enforce the [CFPB]’s rules in areas under their jurisdiction, the same way that states will be permitted to enforce those rules. This co-regulation is further evidenced by the fact that tribes establish their own laws authorizing lending activities within the jurisdiction of their tribal lands and establish regulatory agencies to oversee, require compliance from and regulate tribal lending entities.”

In addition to the argument that Congress intended tribes be regulators, not among the regulated, it can be argued that tribes and tribal entities are not subject to the CFPB’s Section 1021 powers. Section 1021 sets forth the CFPB’s general powers over a “covered person” that offers consumer financial products and services of all types (e.g., mortgages, debit cards, etc.). For the purposes of Section 1021, “covered person” is defined in the Dodd-Frank Act itself, so the CFPB has no power to define it by rule, unlike its express ability to define covered persons subject to its payday lending authority granted in Section 1024. Section 1002(6) defines a “covered person” as “(A) any person that engages in offering or providing a consumer financial product or service; and (B) any affiliate of a person described in subparagraph (A) if such affiliate acts as a service provider to such person.” Section 1002(19) defines a “person” as “an individual, partnership, company, corporation, association (incorporated or unincorporated), trust, estate, cooperative organization, or other entity.”

Based on the above definitions, “covered persons” cannot be governments (i.e., tribes), but they could be tribal entities if the definition is read liberally because of the phrase “any person.” It can be argued, however, that since Congress chose to include tribes expressly in the definition of “State,” as discussed above, which mainly covers preemption but did not choose to include tribes (and by extension, tribal entities) in the definition of “covered persons” or “persons” for the purposes of Section 1021, then the CFPB cannot exercise its power over tribal lending entities (“TLEs”) to require certain disclosures and prohibit practices it deems unfair, deceptive, or abusive. Even if a court does not agree with this

argument, tribal entities will be subject to Section 1021's disclosure and anti-fraud regime but likely will be immune from plaintiffs' suits or state enforcement actions for money damages alleging violations of Section 1021. Instead, tribal entities only would be subject to CFPB enforcement actions for compliance with Section 1021.

Still, even if a tribal entity structures its loans to fall outside of the CFPB's definition of payday loans, and tribes are excluded from the definition of "covered persons" subject to its Section 1021 powers, the CFPB has authority to preempt certain state laws, and tribes are included in the definition of "State." The CFPB's preemption authority allows it to preempt certain tribal laws that may impact the profitability of online lending, but it does not eliminate the tribe's sovereign immunity, and the CFPB cannot regulate the interest an entity charges on its loans.

The CFPB may preempt state laws inconsistent with the provisions of the CFP Act, and then only to the extent of the inconsistency, although the CFPB is expressly forbidden from regulating loan interest rates. Tribes therefore may pass laws allowing loan interest rates to exceed state usury limits without fear of CFPB preemption, although the CFPB may preempt other tribal lending laws. In that manner, aside from being able to charge higher interest rates, tribal lenders would be treated the same as any other lender. For example, if the CFPB promulgates a regulation prohibiting excessive rollover fees, it would have the power to preempt a tribal law allowing such fees.

The CFP Act uses the term "State" 164 times and generally does so within the following four contexts: (i) in requiring the CFPB and states to coordinate with respect to regulating consumer financial products or services; (ii) in requiring the CFPB and states to share reports relating to persons providing consumer financial products or services; (iii) in discussions of state law in the context of preemption and (iv) in definitions and exclusions not relevant to lending. The term "State" is never used in the context of waiving immunity from suit or granting a court jurisdiction to hear a claim. Tribes therefore may engage in lending without waiving their sovereign immunity with respect to state enforcement actions or private plaintiff suits as a result of definitional aspects of the CFP Act.

### *C. TLEs Improve Access to Mainstream Financial Institutions*

Title XII of the Dodd-Frank Act's stated purpose is "to encourage initiatives for financial products and services that are appropriate and accessible for . . . Americans who are not fully incorporated into the financial mainstream." To encourage these initiatives, the Treasury Secretary has the authority, but not the obligation, to establish programs intended to enable low- and moderate-income individuals to establish accounts at insured deposit institutions and enter into low-cost, small loans as alternatives to payday loans. Only certain eligible entities are permitted to participate in these programs and thereby offer such loans and provide related services. The Dodd-Frank Act expressly defines such eligible entities to include "tribal government entities," thereby recognizing that tribal entities may play an important role in consumer finance. The Treasury Secretary, to date, has neither promulgated any rules implementing the programs nor indicated whether the Treasury Department intends to do so. Regardless, by including tribal entities in the definition of eligible entities, Congress has recognized expressly that tribes

have the ability to play an important role in consumer finance. If Treasury decides to move forward with the certain initiatives, it may provide a strong opportunity for tribes to expand their footprint in the financial system.

First, Title XII authorizes the Treasury Secretary to establish a multiyear program of grants, cooperative agreements, and other undertakings with the purposes of (i) enabling low- and moderate-income individuals to establish accounts in a federally insured depository institution and (ii) improving access to such accounts on reasonable terms. Eligible entities, potentially including tribal entities, participating in these programs may provide products and services to low- and moderate-income persons, including small-dollar value loans and financial education and counseling relating to conducting transactions and managing accounts.

Second, Title XII authorizes the Treasury Secretary to establish a multiyear demonstration program to provide low-cost, small loans to consumers as an alternative to more costly payday loans. These loans must be made on terms and conditions and pursuant to lending practices that are reasonable for borrowers. Eligible entities must provide financial literacy education to each borrower provided with a loan pursuant to this program.

#### *D. The Indian Gaming Regulatory Act as an Analogue*

Tribal governments that participate in e-commerce, including legal online lending, are putting these governmental revenues to use in ways that fulfill the mandate of the CRA and which should therefore enjoy full federal government support. The federal legislation that provides a regulatory structure for tribal government gaming, the 1988 Indian Gaming Regulatory Act (“IGRA”),<sup>19</sup> requires that all net gaming revenues be invested in tribal government social and economic recovery, including the federal goals of strengthening tribal self-determination and supporting tribal self-government. Tribal governments participating in the online financial services industry have used this opportunity to create jobs and invest in tribal nation building activities, including health care, education and infrastructure improvements. Many tribes participating in tribal lending have few other options in the wake of federal funding shortfalls and shrinking tribal budgets, and most of them invest their lending revenues in a manner similar to the tribal nation building activities of tribes with gaming.

IGRA clearly states that, “net revenues from any tribal gaming are not to be used for purposes other than-- (i) to fund tribal government operations or programs; (ii) to provide for the general welfare of the Indian tribe and its members; (iii) to promote tribal economic development; (iv) to donate to charitable organizations; or (v) to help fund operations of local government agencies.”

Tribal governments engaged in e-commerce through online lending, whether or not they engage in gaming, have similarly supported nation building in the following ways:

- Employment: creating jobs on tribal land, including financial support

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<sup>19</sup> Indian Gaming Regulatory Act, *hereinafter* “IGRA,” (Pub.L. 100–497, 25 U.S.C. § 2701 et seq.)

staff, Head Start educators, and tribal housing personnel;

- Infrastructure: critical funding for new tribal housing and renovation;
- Education: additional classrooms, books, and teachers for Head Start, new after-school programs, new summer youth programs;
- Tribal Services: child care services, employment training, natural resources, development, financial assistance, utility assistance, healthcare and wellness coverage, emergency assistance;
- Social Services: child protection, low-income Home Energy Assistance Program, family violence protection.

Tribal government e-commerce initiatives do not just support basic, fundamental needs for tribal government operations and services. They also extend the opportunity for tribes to move beyond sheer subsistence and basic economic survival. Internet commerce gives tribal governments hope in their ability to depart from past struggles for survival to legitimate possibilities for continued economic growth, prosperity and success.

While some tribal governments have the necessary human capital to operate online lending ventures without outside managerial assistance, other tribes have had to look outside the tribe for management and/or technical expertise. Such partnering is common for tribal entities entering a new industry and it has succeeded in the past for land-based businesses ranging from tribal gaming management to 8(a) contracting.<sup>20</sup> When tribal governments began to participate in the land-based casino industry, many opponents (and competitors) claimed that tribes did not possess the business or technical skills to operate their properties successfully. Some tribal governments, with approval from the federal government (both the Department of the Interior and the National Indian Gaming Commission, or NIGC) and within a framework described in IGRA, signed agreements with outside management companies to facilitate operations and train tribal members for casino operations management. In addition to formalizing these management relationships, generally for a limited term, tribal governments also contracted with product vendors who supplied technology solutions for slot machine gaming, electronic forms of bingo and other sophisticated games management, products and services. Just as was the case with tribal government gaming, the fact that tribal lending operations initially outsource some of their technology or marketing functions to those with a core competency in those functions. This sound business practice should not de-legitimize the tribal ownership and regulatory oversight of the overall operation.

In addition to tribal investment of lending revenues, tribal co-regulation of gaming with the NIGC has prepared tribal governments for the opportunity presented by the creation and regulation of TLEs on tribal lands. Mobilizing the authority enshrined in the Dodd-Frank Act, tribal governments have established robust regulatory agencies wherein they can partner with other government agencies, including federal agencies like the CFPB, to retain their position as the primary regulators for financial services such as short-term online lending.

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<sup>20</sup> <https://www.sba.gov/content/about-8a-business-development-program>

### *E. An Indigenous Rights Perspective*

Although the analysis in this paper is generally limited to domestic law, it should be noted that the United States has endorsed the United Nations Declaration on the Rights of Indigenous Peoples. Article 9 of the Declaration states that

Indigenous peoples and individuals have the right to belong to an indigenous community or nation, in accordance with the traditions and customs of the community or nation concerned. No discrimination of any kind may arise from the exercise of such a right.<sup>21</sup>

Thus, it would seem entirely inappropriate to deny tribal governments the same abilities to engage in lending that other non-tribal institutions enjoy.<sup>22</sup>

## II. ECONOMIC IMPACT OF TRIBAL ONLINE LENDING

We present the following case studies to exemplify the impact that tribal lending operations have on the respective tribal communities. For most tribes engaged in lending, these operations represent a critical lifeline for tribal government funds. While most tribal governments with lending are also engaged in gaming, it is clear that gaming is not meeting their economic development, employment or community needs. In some instances, tribes have either agreed to be identified or to have their operations discussed publicly. In other cases, tribes have asked that we not disclose their identity.

### *A. Lac Vieux Desert Band of Lake Superior Chippewa*

The Lac Vieux Desert Band of Lake Superior Chippewa located in Watersmeet, Michigan, gained federal recognition in 1988. Their reservation land is geographically isolated on their original homelands ten miles north of the Wisconsin border in Michigan.<sup>23</sup> The tribe is one of twelve bands identified as the Lake Superior Bands of Chippewa Indians.<sup>24</sup> The tribe operates a variety of businesses including construction, day care services, restaurant, fish hatchery, golf course, casino, and consumer financial services including an online lending operation.<sup>25</sup> Employment opportunities outside these ventures are located 30 to 50 miles away from Watersmeet (Frozen Homeland, 2014).

Red Rock Tribal Lending, LLC, and Duck Creek Tribal Financial, LLC,

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<sup>21</sup> Declaration on the Rights of Indigenous Peoples, Article 9 (2008), *available at* [http://www.un.org/esa/socdev/unpfii/documents/DRIPS\\_en.pdf](http://www.un.org/esa/socdev/unpfii/documents/DRIPS_en.pdf)

<sup>22</sup> See discussion of Wells Fargo and USBank, Section III.A. *infra*.

<sup>23</sup> Frozen Homeland. (2015): Native American Financial Services Association. Retrieved from: <https://vimeo.com/91351636>

<sup>24</sup> Lac Vieux Desert Band of Chippewa Indian Community (2012). Intertribal Council of Michigan, Inc. Retrieved from: <http://www.itcni.org/blog/2012/10/11/lac-vieux-desert-band-of-chippewa-indian-community/>

<sup>25</sup> Frozen Homeland

support the online lending ventures of the tribally owned and operated financial service businesses. These high-rate lending enterprises started around 2012 in an industry that has “grown about 20 percent since 2009.”<sup>26</sup> The tribe’s general counsel states, “the revenues generated from the tribal lending entities accounts for about 42% of the general fund budget.”<sup>27</sup> These funds directly support programs such as housing, education, community health clinic, scholarships, and propane assistance. With winter temperatures of 45-47 degrees below zero -- the harshest conditions on record -- propane assistance in 2013 was a necessity to address this major crisis for many tribal members.<sup>28</sup>

### B. Otoe-Missouria Tribe

Originally from the Great Lakes Region of the United States, the Otoe-Missouria Tribe was relocated in 1881 to the northern part of Oklahoma to the town of Red Rock. The tribe reports nearly 3,000 tribal members living in and around Oklahoma.<sup>29</sup>

The tribe’s gaming enterprises fostered investments in ventures including a rural propane company, agriculture operations in cattle and farming, online and convenience stores, and two financial services companies.<sup>30</sup> Tribal Chair John Shotton, states “...the most exciting area we’ve been involved in recently that’s been the most productive in our community has been online, short-term lending and ecommerce opportunities.”<sup>31</sup> American Web Loan and Great Plains Lending are two consumer financial service businesses owned and operated by the tribe. In 2013 Great Plains Lending projected employing 30 tribal and non-tribal employees to staff its call center at full capacity,<sup>32</sup> with another 30 jobs at a separate call center.<sup>33</sup>

At the 2015 Reservation Economic Summit, Chairman Shotton pointed out that the tribe derives 40% of the total tribal government budget from the TLEs and that investment priorities are aligned to meet community needs.<sup>34</sup> The flexibility for investment of tribal lending revenues allows tribal leadership to invest in ways that provide direct benefits to tribal people, unlike federal funds or gaming revenues that have restrictions.

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<sup>26</sup> Harlan, C. (2015 Mar 1). Indian tribes gambling on high-interest loans to raise revenue. Washington Post. Retrieved from: [http://www.washingtonpost.com/business/economy/indian-tribes-gambling-on-high-interest-loans-to-raiserevenue/2015/03/01/8551642d-e51b-4d3a-89c6-4de0d3bdf385\\_story.html](http://www.washingtonpost.com/business/economy/indian-tribes-gambling-on-high-interest-loans-to-raiserevenue/2015/03/01/8551642d-e51b-4d3a-89c6-4de0d3bdf385_story.html)

<sup>27</sup> Frozen Homeland

<sup>28</sup> *Id.*

<sup>29</sup> Otoe & Missouria: Five Hundred Years of History. (2015). The Otoe Missouria Tribe. <http://www.omtribe.org/index.php?culture-history>

<sup>30</sup> Tribal Enterprises (2015). <http://www.omtribe.org/index.php?tribal-enterprises>

<sup>31</sup> Otoe Missouria Tribe. (2014): Native American Financial Services Association. [Video File]. Retrieved from: <https://vimeo.com/62361652>

<sup>32</sup> Otoe Missouria Tribe. (2014)

<sup>33</sup> Comments at 2015 Reservation Economic Summit

<sup>34</sup> *Id.*

Chairman Shotton also discussed how the tribe's use of tribal government revenues from lending has evolved over time.<sup>35</sup> The first year of lending, the tribe invested 100% of revenues into housing renovation. After years of waiting on NAHASDA<sup>36</sup> and other federal funds, the tribe took the lead and renovated housing across the reservation. In the second year, they focused on new housing and created a 20-home addition on the reservation. Next, they invested in tribal programs, including a Head Start program with a new classroom. This program is 100% funded with lending revenues. The funds are also used for building and infrastructure maintenance. While grants or other funding can be used to build building and infrastructure, these buildings cost money to maintain in the long run and the lending revenues are invested in ways that maximize use and longevity of these tribal assets. Investments in elders' services, education, and economic development were also implemented. The Chairman concluded by noting that in addition to the 60 people employed in the call centers, eight full-time employees work in the afterschool program.

The revenues from the online loan companies have made it possible to further invest in the Otoe-Missouria Tribe's efforts of cultural preservation, language revitalization, and support for its warrior society. The Tribal Assistance Program ("TAP") relies exclusively on tribal lending revenues.<sup>37</sup> The purpose of the TAP is

to provide financial assistance to tribal members who are unemployed, economically disadvantaged, disabled or who are experiencing extraordinary circumstances. The Tribal Assistance Program is designed to provide financial assistance for the unmet needs of enrolled members of the Otoe-Missouria Tribe. Assistance is available for housing (mortgage and rental), housing repairs, utilities, dental and medical services, eyeglasses, prescriptions, hearing aids, child care, school expenses, elder assistance and extraordinary assistance. In addition to TAP funds, the tribe created a Housing Department that is funded from the online lending venture that distributes funds directly to members through home improvement options for existing homes and building new homes with green technology and sustainability features. A separate complex of 19 new homes aimed toward home ownership instead of renting will be available to tribal members for purchase at half the cost of construction.<sup>38</sup>

### *C. Habematolel Pomo of Upper Lake Tribe*

The Habematolel Pomo of Upper Lake tribe is located in Upper Lake, California, north of Sacramento. The ancestors of the tribe have been in that region

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<sup>35</sup> *Id.*

<sup>36</sup> Native American Housing Assistance and Self Determination Act of 1996, Public Law 104-330

<sup>37</sup> Comments at 2015 Reservation Economic Summit

<sup>38</sup> Otoe Missouri Tribe. (2014)

of California since at least 6,000 BC.<sup>39</sup> European migration and settlement brought conflict and disease that, in one generation, decimated the tribe's population by 95%, and the "flawed federal policies that ensued subjected Pomo Indian tribes to enslavement, internment, horrific abuse, and slaughter."<sup>40</sup> Notably, in 1950, the U.S. Cavalry nearly eradicated the tribe, particularly elderly, women and children, in an aggressive military operation known as the "Bloody Island Massacre."<sup>41</sup> According to the tribal chairwoman, the "only survivor of that attack was a 6-year old girl who survived by hiding underwater and breathing through a tule reed."<sup>42</sup> Despite the systematic governmental efforts to destroy the tribe and its identity, they persevered and challenged the federal governments genocidal policies in 1975.<sup>43</sup> Although the litigation took nearly 10 years, the tribe prevailed, although the BIA continued to thwart the tribe's attempts at self-determination.<sup>44</sup> Although the ancestral homeland of the tribe once spanned parts of central and northern California, it took until 2004 for the Department of the Interior to finally agreed to accepted into trust a small, 11.24 acres tract of land for the benefit of the tribe.<sup>45</sup> As a result, "[t]oday, federal law permits tribes such as Upper Lake to find a suitable site for restoration of its tribal activities and business operations near its aboriginal tribal lands."<sup>46</sup>

The tribe's initial economic development entity, a casino operation, entered its second year in the early part of 2014,<sup>47</sup> although the gaming facility is not yet profitable. While the tribe hopes that a permanent building to house the gaming operation and potentially a hotel will enhance gaming revenues and begin to generate profits. The tribe currently generates 100% of its governmental budget from a variety of consumer financial services companies they categorize as TLEs. These services include online lending operations, Silver Cloud Lending, Golden Valley Lending, and Mountain Summit Financial. Further, they have embarked on streamlining their lending service operations by acquiring Upper Lake Processing Services, a propriety underwriting system, and Arrowshade, a marketing and lead generation company to support these entities.<sup>48</sup>

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<sup>39</sup> Testimony of Chairwoman Sherry Treppa, Habematolel Pomo of Upper Lake, before the United States House of Representatives Committee on Financial Services, "Short-Term, Small Dollar Lending: The CFPB's Assault on Access to Credit and Trampling of State and Tribal Sovereignty," February 10, 2016, available at <http://financialservices.house.gov/uploadedfiles/hhr-114-ba15-wstate-streppa-20160211.pdf>

<sup>40</sup> *Id.*

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

<sup>43</sup> *Id.*

<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

<sup>46</sup> Habematolel Pomo of Upper Lake. <http://www.upperlakepomo.com/>

<sup>47</sup> Habematolel Pomo of Upper Lake Newsletter, Vol. 13, Issue 1. (2014 Jan –June). <http://www.upperlakepomo.com/forms/HPUL-Arrow-Newsletter-14-01-06.pdf>

<sup>48</sup> Habematolel Pomo of Upper Lake Double Issue Newsletter. Vol. 13, Issue 3. (2015 Mar – 2014 Oct). <http://www.upperlakepomo.com/forms/HPUL-Arrow-Newsletter-14-Oct-15-Mar.pdf>



The tribe's chairperson, Sherry Treppa, states that revenues from TLE-related businesses fund all of the governmental programs including the Honor Elder Assistance Program, the Supplemental Assistance Self Sufficiency Program, the Summer Youth Education Program, the Educational Clothing Allowance Program, Committee Stipend Program, Burial Assistance Program, and Tribal Charity Program. Revenues also supplement the Seven Generations Scholarship Program, culturally based education programs, and acquisition of historically significant tribal lands. Chairperson Treppa also asserts that TLE operations are a key factor in the economic stability of the tribe.<sup>49</sup> In the early 2014, the tribal newsletter reported each TLE exceeding its guaranteed income baseline.<sup>50</sup> At RES2015, Treppa reiterated that 100% of the tribal government budget comes from the TLEs.<sup>51</sup> She also noted that the tribe uses TLE profits to pay down casino debt and for all of their tribal programs, with an emphasis on education, mainly college and adult education and programs, to transition from unemployment to employment.

#### *D. Other Tribal Lenders*

Because of the threat of unwarranted assault from state regulators, other tribes have lending operations but declined to be individually identified for this article. One such tribe, however, did highlight the direct impact of tribal lending on the health and welfare of not only their community but also nearly a dozen other tribes in the surrounding community.<sup>52</sup> Among the tribes in a particular county in California, diabetes rates are nearly 50% among the adult population. One tribal chairman, who has a lifelong devotion to health and fitness, decided that even though his tribe was the smallest in the county, they would pull together the resources necessary for a diabetes and wellness center. That tribe generates no gaming revenues whatsoever, but it does generate revenue from TLEs. In addition to funding government programs, the revenues from the TLEs is also servicing the debt on the loan for the newly constructed diabetes and wellness center, which is now providing services to all of the tribes in the county.

Another tribe in the Midwest operates TLEs not only as a form of economic diversification but also as a source of funds for extending diversification efforts beyond both gaming and lending.<sup>53</sup> One of the goals of tribal government economic development in the gaming era is economic diversification. Because gaming relies upon public opinion and public support, many tribes across the United States, including this tribe, are hesitant to rely solely on gaming for long-term tribal revenues. In terms of government structure, this tribe houses their lending operation within their larger tribal Economic Development Corporation (EDC). The EDC then directs 100% of the tribe's lending revenues into economic diversification efforts. As a result 100% of all new (non-gaming) jobs are a direct result of tribal online lending. Investments of lending revenue by the EDC also extend to the renovation of old or formerly shuttered tribal businesses (e.g. a

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<sup>49</sup> Vol 13, Issue 3

<sup>50</sup> Vol 13, Issue 1

<sup>51</sup> Comments at RES2015

<sup>52</sup> Interview notes on file with Professor Clarkson.

<sup>53</sup> Interview notes on file with Professor Spilde.

smoke shop, convenience store, and grocery store) as well as a strategic restructuring of the tribe's business operations. In addition, the tribe is also breaking ground on a treatment center that will rely on EDC and lending funds for building and maintaining the tribe's long-term commitment to health and wellness in the community.

### III. THE PROBLEM WITH OUTSIDE REGULATION

Because small business drives much of the US economy, an increase in small-business activity is a rational step towards improving employment levels and other aspects of reservation economies. But whether they intend to or not, hostile federal and state officials are attempting to crush the fledgling tribal e-commerce industry, striking a blow to both consumers and tribes. We have seen this scenario at least once before. As Professors Clarkson and Sebenius discussed in an earlier article,<sup>54</sup> when Indian gaming began, state officials were vehemently opposed and fought vigorously to shut down tribal gaming operations. Sometimes they succeeded, but ultimately Indian gaming has emerged as the single greatest economic development strategy in Indian Country. Critical to that tribal victory was the Supreme Court decision in *California v. Cabazon Band of Mission Indians*, where the states were told in no uncertain terms that they had no business regulating on-reservation economic activity when it is not expressly prohibited in the state.

In much the same way, state efforts to regulate or shutter tribal government lending entities severely damage tribal economies while providing little benefit to states. In many cases lending has become the center of a reservation's economy and is one of the most significant employers of tribal members. When lending operations in these communities are forced to shut down, it prevents critical cash resources from flowing directly into the tribal economy. This money is often earmarked for developing other sustainable businesses and infrastructure, and without it, tribes are left in the same dire situation they have been in for decades. Additionally, by eliminating jobs associated with tribal lending, state over-reach leaves the best and brightest tribal members with the excruciating choice of unemployment or community abandonment.

States, in contrast, benefit very little from imposing their laws on tribal lenders. While some state residents may have the opportunity to escape loans they agreed to but could not repay, it should not be a state's prerogative to nullify contracts consummated on reservations. Expending state resources to regulate behavior on reservations that are in some instances thousands of miles away and share no borders with the state is similarly questionable at best. With this perspective in mind, tribal loan controversies pit innovative tribal entrepreneurs who greatly benefit their communities against states limply asserting that they know what is best for tribes and consumers.

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<sup>54</sup> Gavin Clarkson and James K. Sebenius, *A Brief History of Indian Gaming*, New Mexico Business Outlook, March, 2013; See also Clarkson & Sebenius, Missouri L. Rev., *supra* note \_\_\_\_

*A. State Assaults on Tribal Sovereignty*

Looking beyond direct economic effects, state regulation violates the most fundamental tenet of tribal sovereignty: the right of a tribe to govern its land and people. A vast majority of tribes have their own comprehensive bodies of law and adjudicate disputes arising on their territory through tribal courts. If an agreement is entered into on tribal land and involves a tribal member, it is logical that tribal law should apply. To allow application of another sovereign's law to such agreements – which directly implicate the economic well-being of the tribe – is not only counterproductive but is contrary to nearly two centuries of Supreme Court jurisprudence. Yet this overreaching is exactly what states seek to do by regulating tribal lenders. Implicit in this attempted regulation is a fundamental disrespect for tribes. Not only do states assume that tribes cannot sufficiently govern basic loan transactions but also are willing to reach across state boundaries and put their thumb on tribes that have no other connection to the state. In doing so, they violate basic notions of mutual respect that underlie the peaceful co-existence of tribal and state governments, once more with little benefit to show for their efforts.

State regulation also has dire implications for the rights of consumers and businesses. Tribal members structured their lending businesses so they could offer products on the reservation that consumers could not obtain in their respective states. These lenders were open about the fact that only tribal law applied, and consumers willingly agreed that this restriction would be the case. Nevertheless, states are now asserting that the clear, agreed-upon terms are invalid and are trying to ban tribal lenders from offering loans. From an economic perspective, this restriction prevents consumers from accessing products they desire and exemplifies the “nanny state” at its worst. Instead of having the option to enter into loan agreements under tribal law, states are leaving many consumers with no ability to borrow whatsoever.

Perhaps most disturbing about state regulation efforts is their underlying rationale. States have claimed that because borrowers communicated with the tribal lenders through the Internet, state law rather than tribal law must apply. This reasoning cannot be right – if it were, any state could apply its laws to online transactions involving its residents to the exclusion of other sovereigns with even greater interests at stake. It would also mean that tribal sovereignty is a nullity online, a regressive view that conflicts with ongoing congressional efforts to promote tribal economic development and self-sufficiency. Our governmental system, flawed though it may be, cannot abide these irrational legal interpretations.

The states will have to concede that if the borrowers drove the thousand miles to sign the paperwork on the reservation, state law would not apply, but to require such inefficient economic transaction costs of two poor counterparties smacks of the same racist notions that have been pervasive whenever Indians and Indian tribes have attempted to use advanced technology to compete in modern society. The same rhetoric was used when animal rights activists attempted to deny Alaskan natives or Makah Indians their inherent rights to engage in subsistence whaling – it wasn't being “traditional” to use guns to kill the whale, only hand-

thrown harpoons were acceptable.<sup>55</sup>

Now, many state regulators are arguing that tribal governments shouldn't be able to offer lending products over the Internet when larger non-Indian enterprises can legally export interest rates on credit cards and loans with impunity. When we conducted a quick APR calculation of payroll advance lending by major banks, the rates ranged between 651% and 1,303%,<sup>56</sup> yet we are unaware of state regulators attacking Wells Fargo or USBank for offering loan products with rates far higher than those offered by Indian Country lenders. The ability of banks and credit card companies to charge interest to out-of-state borrowers based on rates permitted in states in which they are chartered was settled more than 35 years ago in *Marquette Nat'l Bank v. First Omaha Serv. Corp.*<sup>57</sup> That decision, coupled with subsequent Congressional action,<sup>58</sup> fundamentally transformed the credit card industry by allowing banks and credit card issuers to export nationally whatever interest rate is allowed in the state in which they are headquartered, regardless of the law where the borrower resides. South Dakota allows banks and credit card issuers to offer unlimited interest rates to New York customers (as does Delaware), but according to New York's regulators, apparently tribes in Oklahoma shouldn't be able to offer similar financial products.

According to the FDIC, consumers "need . . . responsible small-dollar loan products."<sup>59</sup> State and federally chartered banks have a long history of offering credit consistent with US federal law, including the extension of small-dollar, short-term credit. These loans are offered by some banks and expressly *encouraged* by the FDIC.<sup>60</sup> Equal treatment should be accorded to small-dollar credit offered by non-depository lenders making loans consistent with applicable US federal and tribal laws, specifically when these loans are offered by tribal governments along the following terms:

- Fully Disclosed. Loans made by tribal governments are made consistent with the federal Truth in Lending Act and provide disclosure of all material loan terms, including the APR, finance charge, schedule of payments and total payments.
- Authorized. Loans made by tribal governments are made consistent

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<sup>55</sup> See e.g. <http://www.nytimes.com/2011/10/17/us/in-sacred-whale-hunt-eskimos-use-modern-tools.html>

<sup>56</sup> According to Professor Clarkson's analysis in 2013, Wells Fargo charged \$1.50 per \$20 borrowed or \$7.50 per \$100 borrowed, so borrowing \$500 for 14 days results in a payback of \$537.50 or an APR of 977%. US Bank charged \$2 per \$20 borrowed or \$10 per \$100 borrowed, so borrowing \$500 for 14 days results in a payback of \$550 or an APR of 1303%. See Gavin Clarkson, "Nanny-State Regulators: The New "Deadliest Enemies" for Economic Development in Indian Country," New Mexico Business Outlook, November 2013.

<sup>57</sup> 439 US 299 (1978)

<sup>58</sup> See National Bank Act, 12 USC 85 and 12 CFR 7.4001

<sup>59</sup> Oral Statement of Mark Pearce, Director, Division of Depositor and Consumer Protection, Federal Deposit Insurance Corporation on Payday Loans: Short-Term Solution or Long-Term Problem to the Special Committee on Aging, U.S. Senate (July 24, 2013).

<sup>60</sup> <http://www.fdic.gov/small-dollar-loans/>

with the federal Electronic Funds Transfer Act. Accordingly, the offering of credit is not conditioned on repayment by recurring debits. Rather, the consumer authorizes the debit in a specific dollar amount to be debited on a certain date from a specific bank account.

- Not “Evergreen.” Loans made by tribal governments are generally structured as short-term installment loans. As such, the loan has a maturity date and does not automatically roll over, extend, or renew.

#### *B. Tribal Consumer Protection Best Practices*

It is also highly problematic that regulators assume that tribal online lenders lack the capability to regulate appropriately. As with Indian gaming, tribal nations have repeatedly demonstrated their capability to regulate activities involving non-Indians, often in a manner superior to those put forward by federal or state regulators. When the United States House of Representatives Committee on Financial Services held a hearing on February 10, 2016, the topic of the hearing was appropriately identified as “Short-Term, Small Dollar Lending: The CFPB’s Assault on Access to Credit and Trampling of State and Tribal Sovereignty.” Chairwoman Sherry Treppa testified not only in her capacity as a tribal representative but also as the Vice-Chairperson of the Native American Financial Services Association (“NAFSA”). In those hearings, she detailed a very sophisticated consumer protection regime consistent with the best practices put forward by NAFSA,<sup>61</sup> noting that

From our sovereign power springs the right to legislate and regulate the operations of business activities within our jurisdiction. Consistent with our commitment to improve our members’ economic prospects, in 2010, the Tribe began to explore e-commerce and online small dollar lending as a viable economic opportunity. After a thorough review of the industry and related opportunities, our tribal council, consistent with our inherent power, constructed a regulatory framework using the model that has proven successful in the tribal gaming industry.<sup>62</sup>

She then detailed how the tribe passed lending laws setting forth the parameters of legal operation of consumer lending from within the reservation, specifically noting that tribal law prohibits TLEs from “engaging in unfair, deceptive, or fraudulent practices, or engaging in any consumer financial services other than those expressly permitted under that ordinance. [TLEs] that issue loans within [the reservation] must comply with that legislation.”<sup>63</sup>

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<sup>61</sup> <http://www.mynafsa.org/best-practices/>

<sup>62</sup> Testimony of Chairwoman Sherry Treppa, Habematolel Pomo of Upper Lake, before the United States House of Representatives Committee on Financial Services, “Short-Term, Small Dollar Lending: The CFPB’s Assault on Access to Credit and Trampling of State and Tribal Sovereignty,” February 10, 2016, available at <http://financialservices.house.gov/uploadedfiles/hhrg-114-ba15-wstate-streppa-20160211.pdf>

<sup>63</sup> *Id.*

Chairwoman Treppa then described the creation of a regulatory commission charged with oversight of the TLEs and given the power to enforce tribal laws.<sup>64</sup> She emphasized that the regulatory commission is a separate instrumentality of the tribe, operating independently of the political arm of the tribal government, noting that “The commission has the autonomy to exercise its enforcement authority should a [TLE] violate the consumer protection laws that we established.”<sup>65</sup>

Chairwoman Treppa’s testimony then turned to a discussion of how the Habematolel Pomo Indians of Upper Lake exercises their sovereign power in other ways beyond just their

robust legal and regulatory framework. We have actively sought opportunities to enter into cooperative agreements or compacts with states as a means to coordinate the exercise of authority in this area and promote a collaborative government-to-government regulatory environment. By way of example, our Tribe successfully entered into a Memorandum of Understanding with the State of New Mexico in December, 2014, which explicitly memorialized our Tribe’s sovereign authority to engage in online short-term lending and acknowledged that the legislation enacted by our Tribe effectively regulates transactions between consumers and licensed lenders that occur on Trust land, adheres to best practices, and does not violate federal or tribal law.

She then described the California Department of Business Oversight’s Information-Sharing Pilot program, a collaborate effort between state regulators, her tribe, and other tribal members of NAFSA, which is exploring

opportunities to develop a framework that facilitates information exchanges between regulatory authorities. The experience was positive, and we continue to pursue open dialogues and additional Memoranda of Understanding with other states, ever eager to work cooperatively and communicate openly with states as co-regulators to achieve shared goals of consumer fairness and protection. Indeed, these efforts are consistent with the regular practice of many Tribes throughout the country to collaborate with state authorities on tribal-state relations in areas as wide ranging as law enforcement, environmental protection, hunting and fishing, public lands management, and education.

As evidence that existing law is sufficient to protect consumers,

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<sup>64</sup> *Id.*

<sup>65</sup> Testimony of Chairwoman Sherry Treppa, Habematolel Pomo of Upper Lake, before the United States House of Representatives Committee on Financial Services, “Short-Term, Small Dollar Lending: The CFPB’s Assault on Access to Credit and Trampling of State and Tribal Sovereignty,” February 10, 2016, available at <http://financialservices.house.gov/uploadedfiles/hhrg-114-ba15-wstate-streppa-20160211.pdf>

Chairwoman Treppa noted that an additional “enforcement power available to Tribes in regulating financial services businesses, as the CFPB itself admits, is the ability to bring legal actions under the Dodd-Frank Act, just as States can.”

<sup>66</sup> She then described how in 2015 the Navajo Nation brought an enforcement action, together with the CFPB, against a tax refund business under this authority.<sup>67</sup> On behalf of Upper Lake, she stated that

While we have not seen the need to rely upon anything more than our own laws and regulatory commission to handle consumer complaints and other regulatory issues, my Tribe (and others operating small dollar lending businesses) are aware of this significant power, and are certainly prepared to exercise it should the need to do so arise. This Committee should make no mistake – ample power already exists for Tribes to protect consumers and regulate businesses within its jurisdiction.<sup>68</sup>

To fully illustrate what the Upper Lake Pomo had developed to meet the needs of both consumers and tribal members, Chairwoman Treppa then proceeded to detail their lending operations and obligations under Tribal law. TLEs “must be licensed by our Tribal regulatory commission before they may engage in lending.”<sup>69</sup> TLEs may not charge consumers application fees or penalize them for early repayment.<sup>70</sup> TLEs “must maintain a compliance management system to ensure compliance with Tribal law, promulgated regulations and applicable federal law.”<sup>71</sup> The required TLE systems “must include a full suite of written policies that covers all aspects of lending. Each lender must also have internal controls and processes that allow it to monitor its operations to ensure that its procedures follow those policies.”<sup>72</sup> Additionally, the Upper Lake regulatory commission regularly audits TLEs.<sup>73</sup> If the commission identifies deficiencies during an audit, “or if a lender fails in any way to satisfy their compliance obligations, then the commission is empowered to take corrective action.”<sup>74</sup> The commission’s power “includes imposing fines and penalties, as well as suspending and revoking the lender’s license, which would terminate the lender’s ability to extend credit. This regulatory framework is what our tribal lending entities operate under, and it ensures that their practices are responsible and based on principles of consumer protection.”<sup>75</sup>

Chairwoman Treppa then highlighted a very important distinction between

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<sup>66</sup> *Id.*

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*

<sup>70</sup> *Id.*

<sup>71</sup> *Id.*

<sup>72</sup> *Id.*

<sup>73</sup> *Id.*

<sup>74</sup> *Id.*

<sup>75</sup> *Id.*

the types of loans offered by NAFSA members, including the Upper Lake Pomo, and payday loans. Unlike payday loans, loans authorized under Upper Lake tribal law “are unsecured loans that are repaid in installments, which means our lenders have no real remedies if a customer defaults. Consequently, a robust underwriting process is an operational imperative.”<sup>76</sup> The TLEs operating at Upper Lake

use computer algorithmic waterfalls and data analytic tools to assess a consumer’s application. The amount of a customer’s credit request is compared against their income and existing credit obligations because it is a strong factor in determining their ability to repay. An applicant’s repayment history is checked because it is the strongest factor in assessing their willingness to repay. If a customer’s ability to repay or willingness to repay do not meet the lending company’s underwriting requirements, or if the identity verification portion fails, then the application will be denied.

She then shared data from the TLEs to illustrate the rigor and effectiveness of their underwriting.<sup>77</sup> Only 3.1% of 2015 applicants were accepted.<sup>78</sup> Of those applicants accepted for review, “less than 2% were approved and funded.”<sup>79</sup> In other words, 98.3% of potential new customers were rejected as a result of the underwriting process.<sup>80</sup> Chairwoman Treppa then noted that Upper Lake’s “commitment to responsible lending helps to prevent customers from taking loans they are unable to repay.”<sup>81</sup>

Chairwoman Treppa then proceeded to dispel misplaced notions of the consumers that their TLEs serve, noting that their average customer that is approved for credit is typically “45 years old with a median income of \$45,000 [and] rarely reports public assistance or other benefits as an income source.”<sup>82</sup> The median loan amount is typically “\$700, and, although the installment contract is structured on a ten-month payment schedule, customers are encouraged to pay extra toward the principal or pay off the loan early without penalty.”<sup>83</sup> The Upper Lake regulatory commission has “significant data that shows customers frequently repay their loans in less than four months. Data also shows that our customers have moderate borrowing patterns: when measured over two years, our customers have an average of 1.6 loans.”<sup>84</sup>

After detailing the financial impact to her tribe and the myriad of programs funded by TLE operations, Chairwoman Treppa concluded her prepared

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<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

<sup>80</sup> *Id.*

<sup>81</sup> *Id.*

<sup>82</sup> *Id.*

<sup>83</sup> *Id.*

<sup>84</sup> *Id.*



remarks with a discussion of Upper Lake's commitment to consumer protection.

For American consumers, our credit products offer options for meeting financial obligations without fear of defaulting on an obligation, failing to pay a bill, or overdrawing their checking account. The CFPB may consider small dollar lending to be a scourge of the credit industry; our customers tell a different story. In 2015, our total complaint rate was only 1.6%. This number likely drops to 1% when considering that some of those complaints are likely due to loan applications we denied. That number is significant and it illustrates the quality and the legitimacy of our operations.

My tribe agrees that consumer protection should be a primary concern of this industry, because responding to consumer demand in a regulated, compliant, and helpful manner is the essence of consumer protection – and that is what we do. Much of the reason we have been successful is the strong commitment we have made to ensure that tribal lending businesses adhere to fair and responsible lending practices that protect consumers.<sup>85</sup>

After both her written and oral testimony, many of the committee members questioned the need for CFPB regulation in this arena, and a heated discussion followed about whether CFPB was overreaching in its attempts to regulate tribal government online lending.

### *C. State and Federal Assaults on Tribal E-Commerce*

The continued assault by state and federal regulators on tribal online lenders clearly discriminates against tribal courts and tribal entrepreneurs that select tribal courts and tribal law in their electronic commerce endeavors off-reservation. The potential damage extends beyond tribal online lending and, in fact, imperils all tribal attempts at e-commerce. For example, Professor Clarkson is currently working with the Native American Business Students Association at New Mexico State University to develop an online marketplace to connect Indian artisans with potential off-reservation purchasers. Many of these native artisans have little or no experience with e-commerce, and almost all of them are below the poverty level. If an American Indian artisan is asked through the exchange to produce a piece of jewelry by a potential non-Indian from Illinois, it is perfectly reasonable for the parties to incorporate into their contract that disputes will be settled in tribal court and under tribal law. Under the new rule imposed by the 7<sup>th</sup> Circuit,<sup>86</sup> however, such forum selection and choice of law provisions would be inapplicable if the non-Indian purchaser does not travel nearly 1,500 miles to physically enter the reservation. Instead, in order to pursue a legal remedy, the 7<sup>th</sup> Circuit expects the

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<sup>85</sup> *Id.*

<sup>86</sup> *Jackson v. Payday Financial*, <https://turtletalk.files.wordpress.com/2014/08/ca7-opinion.pdf>

artisan to travel that same distance, at her own expense, or hire an attorney in a jurisdiction that she has never visited, simply because she is an Indian living on a reservation. No other business in the United States is subject to such an arcane requirement in selecting its preferred forum and choice of law. It is improper and discriminatory for the 7<sup>th</sup> Circuit to impose such a restriction on a tribal artisan, or any reservation-based business.

Furthermore, well-established Congressional policy<sup>87</sup> and Supreme Court jurisprudence<sup>88</sup> show strong support for tribal economic development, which the 7<sup>th</sup> Circuit has substantially impaired. If extended to other circuits, this new rule would thwart federal e-commerce efforts already underway as part of the National Broadband Plan, such as Fast-Forward New Mexico, which helps Navajo and Pueblo Indians develop e-commerce capabilities.<sup>89</sup>

As more and more states continue to legalize online gambling, a logical concern arises given that tribes have been exploring online gaming as well.<sup>90</sup> As discussed earlier, tribes have fought long and hard to exercise their sovereign right to conduct gaming on their reservations. Will the same overly aggressive regulators who seek to trample on tribal sovereignty in the e-commerce arena similarly attempt to stifle tribal online gaming?

#### CONCLUSION

Tribal governments are beginning to engage in a range of e-commerce activities ranging from play-for-fun gaming sites to robust online lending businesses. As these activities become more successful and spread across Indian Country, state governments and the federal government become more involved in monitoring and in some cases attempting to exert regulatory authority over tribal e-commerce. E-commerce is the great equalizer for tribal economic development and should not be frustrated by state government interference or attacks on tribal sovereignty by those who oppose the online lending industry in general or tribal sovereignty in particular.

As a matter of law and policy, tribal lending businesses should be permitted to offer loans that are governed by tribal law without fear of state regulation. States exist to serve the people, and it is not in the people's best interest to deny them access to financial products, refuse to enforce their agreements, or destroy the

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<sup>87</sup> See e.g. *Felix Cohen's Handbook of Federal Indian Law* (Nell Jessup Newton ed., 2012), § 21.04 Government Programs to Promote Development (listing numerous federal programs promoting tribal economic self-sufficiency)

<sup>88</sup> See e.g. *Michigan v. Bay Mills Indian Cmty.*, 134 S. Ct. 2024 2043 (2014) (Sotomayor, J. concurring) (““A key goal of the Federal Government is to render Tribes more self-sufficient ... rather than relying on federal funding””)

<sup>89</sup> See Federal Communications Commission, National Broadband Plan, p. 170 (March 17, 2010) available at <http://transition.fcc.gov/national-broadband-plan/national-broadband-plan.pdf>

<sup>90</sup> Rob Capriccioso, *Internet Tribal Gaming Group Tests the Waters*, Indian Country Today, April 2, 2014, available at <http://indiancountrytodaymedianetwork.com/2014/04/02/internet-tribal-gaming-group-tests-waters-154292>

industry of friendly, developing economies.

Academic research challenges policy makers and the financial services industry to focus on foundational causes for the inability of many Americans to live within their means. As former treasury official Sheila Bair has noted,

The escalating demand for the [payday loan] product reflects the woeful inability of millions of Americans to effectively manage their finances and accumulate savings. As long as the demand for short-term credit remains high among high-risk, low-income borrowers, it is unlikely that the payday lending problem will be entirely solved by measures focused on the firms supplying such loans.<sup>91</sup>

Consumers of short-term loans are often overlooked in the debate over increasing access to and healthy competition for these tribal online lending services. When states or business competitors attempt to frustrate tribal governments' legal participation in this industry, these under-served consumers lose. Rather than restrict tribal participation in this legal industry, the public (and public policy) would be better served by addressing the financial mismanagement, high unemployment, and other fiscal conditions that create a growing market for these products in the first place.

More importantly tribal sovereignty should remain available as a development tool in the digital age as it has in the past. It is well established in federal law and policy that state laws should not take precedence over tribal law, and this relationship should not change automatically just because the Internet is involved. Looking back years from now, it will be inconceivable to think that states claimed to have had the authority to regulate loans made in distant reservations. It is hoped that we will not have to wait that long before regulators realize that their actions are fundamentally wrong.

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<sup>91</sup> Bair, Sheila. *Low-Cost Payday Loan: Opportunities and Obstacles*. The Annie E. Casey Foundation, June 2005.