
IN THE
Supreme Court of Indiana

No. _____

Court of Appeals Cause No. 49A02-0711-CV-987

FOUNDATIONS OF EAST CHICAGO, INC.,)	Appeal from the
successor by merger to EAST CHICAGO)	Marion Superior Court
COMMUNITY DEVELOPMENT)	
FOUNDATION, INC. and TWIN CITY)	Cause No.
EDUCATION FOUNDATION, INC.,)	49D13-0705-PL-019348
)	
Appellant (Plaintiff Below),)	The Honorable
)	S.K. Reid, Judge
v.)	
)	
CITY OF EAST CHICAGO,)	
)	
Appellee (Defendant Below), and)	
)	
STATE OF INDIANA,)	
)	
Appellee (Intervenor-Defendant)	
Below).)	

**COMBINED RESPONSE OF THE STATE OF INDIANA TO
THE PETITION TO TRANSFER AND THE MOTION TO CONSOLIDATE**

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STATEMENT OF THE ISSUE

Whether, consistent with the state and federal constitutions, the General Assembly may authorize a municipality to cancel a regulatory agreement directing casino gambling revenue intended for public economic development to private foundations.

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**COMBINED RESPONSE OF THE STATE OF INDIANA TO
THE PETITION TO TRANSFER AND THE MOTION TO CONSOLIDATE**

The State of Indiana, as Intervenor-Defendant and Appellee, respectfully submits this combined response to the Petition to Transfer and Motion to Consolidate, both of which have been filed by the Foundations of East Chicago, Inc. (“FEC”). It is the position of the State that the Court should deny the Motion to Consolidate and hold the Petition to Transfer in abeyance pending its decision in *City of East Chicago v. East Chicago Second Century, Inc.*, 878 N.E.2d 358 (Ind. Ct. App. 2007), *trans. granted*, 898 N.E.2d 1219 (Ind. 2008) (“*East Chicago I*”). Without assuming any particular outcome or rationale in *East Chicago I*, the State also respectfully submits that, once the Court issues its decision in that case, it should choose one of the following options for this case: (1) deny the Petition outright; (2) grant the Petition and remand the case to the Court of Appeals for further consideration in light of *East Chicago I*; or (3) call for further briefing from the parties so that they may appropriately address the significance of *East Chicago I*, if any, for this case.

BACKGROUND AND PRIOR TREATMENT OF THE ISSUES

Viewed most narrowly, this is one of three cases involving a Local Development Agreement (“LDA”) between the City of East Chicago and the local riverboat casino licensee, under which the licensee agreed to distribute 1% of its gaming revenues to the City; 0.75% to East Chicago Second Century, Inc., a for-profit entity; and 1% each to two non-profit entities, Twin City Education Foundation and East Chicago Community Development Foundation (these have

since merged into the current FEC). Appellant's App. Vol. IX at 1634-36. This 3.75% share of the riverboat's revenues was intended to benefit local economic development in the City of East Chicago, as required by statute. See Ind. Code §§ 4-33-1-2; 4-33-6-7(b). More broadly, however, this case can be properly understood only in context with the larger story of extraordinary public corruption that has plagued the City of East Chicago at least since the Indiana Gaming Commission first issued a license for riverboat casino gambling in that city in the mid-1990s.

1. While the Indiana Gaming Commission has ultimate responsibility for awarding a license for a riverboat casino to operate in the City of East Chicago, the Mayor of the City of East Chicago in the mid 1990s, Robert Pastrick, exercised substantial influence over that decision by deciding to back one or another license applicant, ostensibly based on the applicant's commitment to local economic development. 68 Ind. Admin. Code 2-1-5(c)(4). So, beginning in the fall of 1993, former Mayor Pastrick negotiated a deal on behalf of East Chicago with Showboat Casino, whereby Showboat would contribute a portion of its adjusted gross revenues to various economic development projects in return for the City's endorsement of Showboat before the Indiana Gaming Commission. Appellant's App. Vol. IX at 1633-45. Through this deal (commonly referred to as the "Showboat Agreement" or the "LDA"), Showboat agreed to contribute 3% of its adjusted gross revenue, split evenly among the City of East Chicago and FEC's two predecessor foundations. Additionally, Showboat agreed to fund and own a private, for-profit corporation,

East Chicago Second Century, Inc., that would receive a 0.75% share of the casino's adjusted gross revenue. Appellant's App. Vol. IX at 1635-36.

The memorialization of the LDA was subject to the ratification of the Common Council of East Chicago. Appellant's App. Vol. IX at 1641. The Common Council ratified the LDA on September 10, 1995. Appellant's App. Vol. XI at 2220.

Based in part on Pastrick's support for Showboat, the Indiana Gaming Commission issued a Certificate of Suitability for a Riverboat Owner's License in East Chicago on January 8, 1996. Appellant's App. Vol. XI at 2218. While the statutory scheme for granting licenses contemplates competitive bidding, only Showboat applied for the East Chicago license. Appellant's App. Vol. XI at 2218. Showboat began operations on April 18, 1997. *Third Year Evaluation of Riverboat Licensee for East Chicago, Indiana*, Center for Urban Policy and the Environment, School of Public and Environmental Affairs, 1, available at <http://www.in.gov/igc/files/harrahs-3.pdf>.

In 1998, Harrah's Entertainment, Inc., purchased the interests of the various partners in the Showboat Marina Casino Partnership and continued to operate the East Chicago riverboat under the Showboat name. Appellant's App. Vol. XI at 2220. The Commission approved transfer of Showboat's East Chicago license to Harrah's. Appellant's App. Vol. XI at 2222. Later, in December of 1998, Showboat, Waterfront Entertainment and Development, Inc., and two of Mayor Pastrick's friends, Michael Pannos and Thomas Cappas, reached a side agreement, devoid of any Common council approval, providing that the city had the option to transfer

ownership of Second Century to itself, continue to require Showboat to own Second Century, or transfer ownership of Second Century to Cappas, Pannos and Waterfront. Appellant's App. Vol. XI at 2221. Then, in a document dated February 26, 1999, a representative of the Pastrick administration, John D. Artis, Executive Director of East Chicago Development, agreed to transfer Second Century to Pannos and Cappas, again without Common Council approval. Appellant's App. Vol. XI at 2222. The same day, at a hearing before the Indiana Gaming Commission, Artis requested authority for the Pastrick administration to oversee Second Century developments while the Commission oversaw Second Century's spending. Appellant's App. Vol. XI at 2222. However, "[a]fter discussion, the Commission decided there would not be a need for the Commission to play any type of regulatory role in overseeing Second Century." Appellant's App. Vol. XI at 2222.

2. Meanwhile, investigative efforts of the Indiana Attorney General and the United States Attorney for the Northern District of Indiana uncovered a web of official abuse and misconduct so pervasive that it led the Attorney General to file a complaint in federal court in the Northern District of Indiana in August, 2004, against former Mayor Pastrick and numerous appointees in his administration alleging that the City of East Chicago itself was being operated through a pattern of racketeering activity. Appellant's App. Vol. XII at 2419-81. The Attorney General's investigation and his federal RICO complaint focused on the use of millions of dollars of public funds, including economic development funds generated by the East Chicago riverboat, to pay for non-public concrete sidewalk work and other

perks that were doled out to curry political favor and buy votes in order to influence the 1999 and 2003 East Chicago mayoral primaries. Appellant’s App. Vol. XII at 2419-81. This massive abuse of public trust became known as the “Sidewalks for Votes” scandal.

3. In the months following the Attorney General’s filing of the RICO complaint, the East Chicago scandals began to unfold on other fronts. Amid accusations of rampant vote fraud in the 2003 East Chicago Democrat Party primary—the same primary affected by the Sidewalks for Votes scheme involving casino gambling revenue—this Court in *Pabey v. Pastrick*, 816 N.E.2d 1138 (Ind. 2004), ordered a special East Chicago Democratic Party mayoral primary election, where East Chicago Democrats nominated George Pabey, and not Robert Pastrick, as the party’s candidate. Pabey, opposed by Republican Arthur Santos, was elected Mayor of East Chicago at another special election held on December 27, 2004. *E.C. overwhelmingly votes for Pabey*, Northwest Indiana Times, Dec. 28, 2004.

Also that fall, on October 12, 2004, Harrah’s requested that the Commission approve transfer of the license to yet another company, RIH Acquisitions IN, LLC d/b/a Resorts East Chicago (“Resorts”). Appellant’s App. Vol. XI at 2223. However, on March 10, 2005, East Chicago, now under the administration of George Pabey, formally requested that the proposed transfer of the East Chicago Riverboat license from Harrah’s to Resorts be denied unless the payment of economic development funds to the Foundations and Second Century was terminated. Appellant’s App. Vol. XII at 2582.

On April 21, 2005, the Commission conducted a hearing concerning the license transfer request where the City of East Chicago raised concerns about the payment of economic development funds to Second Century and the Foundations. Appellant's App. Vol. XI at 2223. The City alleged to the IGC that FEC and Second Century had "misappropriated and misused funds, violated their respective by-laws and rules and engaged in practices which undermined their respective missions." Appellant's App. Vol. XII at 2582.

Six days prior to that hearing, however, Second Century had initiated a lawsuit seeking a declaration that the payments could not be terminated. Appellant's App. Vol. XI at 2223. Consequently, at the April 21 Commission hearing, Second Century's counsel urged that the courts, and not the Commission, constituted the appropriate forum for arguments concerning the validity of the agreements channeling riverboat gambling revenues intended for economic development to Second Century and the Foundations. *See Interim Investigative Report of East Chicago Second Century, Inc. Conducted at the Request of the Indiana Gaming Commission (2006), Exhibit 8, available at <http://www.in.gov/attorney-general/press/20060608.1.pdf>.*

Apprised of Second Century's newly-filed declaratory judgment action concerning the LDA's validity, the IGC approved the transfer without commenting on the LDA while also requesting an investigation by the Attorney General to determine whether performance of the Showboat Agreement was "consistent with the stated purpose of Indiana's Riverboat Gambling Act and maintain[ed] the

integrity of the riverboat gambling industry[.]” Appellant’s App. Vol. XII at 2581; *East Chicago I*, 878 N.E.2d at 366. The investigation by the Attorney General uncovered that the whereabouts of much of the approximately \$16 million that Second Century had received could not be determined because of obfuscation by Second Century. Appellant’s App. Vol. XI at 2216.

In response to the Attorney General’s report, the IGC passed Resolution 2006-58 on June 8, 2006, disapproving that provision of the Agreement requiring the riverboat casino licensee to make payments to Second Century. Appellant’s App. Vol. XIV at 2878-80. The licensee, now Ameristar Casinos, Inc., has since deposited into a segregated bank account all subsequent payments ostensibly owed under the Agreement to Second Century. *See East Chicago Second Century, Inc. v. RIH Acquisitions IN, LLC d/b/a Resorts East Chicago*, No. 49D01-0706-PL-022673 (Marion Sup. Ct. Dec. 10, 2007) (order on motion to stay).

4. With its revenue stream dried up, Second Century filed a petition for judicial review challenging IGC Resolution 2006-58. *East Chicago I*, 878 N.E.2d at 367-68. Second Century’s petition for judicial review is one component of the litigation referred to throughout these proceedings as *East Chicago I*. The other component of *East Chicago I* is the lawsuit filed by Second Century against Resorts East Chicago (“Resorts”) seeking to enforce the LDA against Resorts; the City of East Chicago intervened in that action in order to ask the court to declare the LDA invalid on various grounds. *Id.* The trial court consolidated the contract action with the judicial review action, and the consolidated case, now before this Court on

interlocutory appeal, has proceeded through the courts as *East Chicago I*. *Id.* at 370.

The Marion Superior Court ruled in *East Chicago I* that the LDA constituted an enforceable contract. *Id.* at 371. Specifically, the trial court held that the LDA is valid, that the predecessors of FEC were third-party beneficiaries, and that the City could not reform the agreements. *Id.* at 370-78. The court noted that “[w]hile East Chicago and the Attorney General argue that allocating large amounts of economic development funding without stringent oversight is unwise, this argument does not satisfy the stringent requirements necessary to overcome Indiana’s strong preference for freedom of contract.” Appellant’s App. Vol. IX at 1650. The trial court did not reach the judicial review petition before certifying its orders in the contract action for immediate interlocutory appeal. The Court of Appeals affirmed the lower court decision in relevant part, and this Court granted transfer. *Id.* at 370-78, 382.

5. In *East Chicago II*, the Attorney General sought the imposition of a constructive trust over the funds that had been paid to Second Century under the LDA, as well as an accounting of how the funds were spent. *Zoeller v. East Chicago Second Century, Inc.*, 904 N.E.2d 213 (Ind. 2009) (“*East Chicago II*”). The trial court dismissed the Attorney General’s claims and the Court of Appeals affirmed the dismissal. *Carter v. East Chicago Second Century, Inc.*, 881 N.E.2d 1114 (Ind. Ct. App. 2008). This Court granted transfer and reversed the trial court’s dismissal, holding that the Attorney General could allege constructive trust claims against

Second Century and seek an accounting. *East Chicago II*, 904 N.E.2d at 217. The Court ruled in that case that the LDA was “not like an ordinary commercial contract at all[,]” but rather, “a mode of implementing the casino’s obligation to contribute to local economic development.” *Id.* at 221. That case is now pending in Marion Superior Court before Judge David Shaheed.

6. While *East Chicago I* was pending in the Court of Appeals and *East Chicago II* was still in the trial court, the Indiana General Assembly passed Section 302 of the Budget Act of 2007, which gave rise to the instant case. Section 302 amended Indiana Code § 4-33-6-7 by adding the following:

(c) This subsection applies to an owner’s license issued for the City of East Chicago. If a controlling interest in the owner’s license is transferred, the fiscal body of the City of East Chicago may adopt an ordinance voiding any term of the development agreement (as defined by IC 36-1-8-9.5) between: (1) the city; and (2) the person transferring the controlling interest in the owner’s license; . . . The ordinance may provide for any payments made under the redevelopment agreement, including those held in escrow, to be redirected to the City of East Chicago for use as directed by ordinance of the city fiscal body. . . .

H.E.A. 1001, 115th Gen. Assembly, 1st Reg. Sess. (Ind. 2007). Thus, Section 302 expressly authorized the City to void or modify the terms of the LDA that existed between it and the riverboat casino licensee upon the transfer of the license.

On October 9, 2007, the City passed ordinances directing funds payable to Second Century and FEC under the LDA to be paid to the City. Appellant’s App. Vol. X at 2053-59. At the direction of the *East Chicago I* and *III* trial courts, these funds are currently being held in separate interest-bearing accounts managed by the casino operator pending the outcome of both cases. *See Foundations of East*

Chicago, Inc. v. City of East Chicago, No. 49D13-0705-PL-019348 (Marion Sup. Ct. Dec. 3, 2008) (order granting interpleader); *East Chicago Second Century, Inc. v. RIH Acquisitions IN, LLC d/b/a Resorts East Chicago*, No. 49D01-0706-PL-022673 (Marion Sup. Ct. Dec. 10, 2007) (order on motion to stay).

In response to the enactment of Section 302, FEC filed this lawsuit, *East Chicago III*, challenging the validity of Section 302 under numerous provisions of the Indiana and United States Constitutions. See Appellant's App. Vol. I at 2. The Indiana Gaming Commission (represented by the Attorney General) was originally a defendant, but on September 12, 2007, FEC stipulated to the dismissal of the IGC from the lawsuit. Appellant's App. Vol. I at 4-5. The Attorney General, on behalf of the State, then intervened in the action to defend Section 302's validity. Appellant's App. Vol. 1 at 4. The Marion Superior Court rejected all of the state and federal constitutional arguments put forth by FEC and held that Section 302 was a constitutional exercise of legislative authority. Appellant's App. Vol. I at 11-63. In particular, the trial court concluded, in language echoed by this Court's decision in *East Chicago II*, that the LDA is "not [a] commercial contract[] whatsoever – rather, [it is] a means of regulating the riverboat licensee by ensuring the statutorily required economic development occurs and it occurs for the benefit of the public." Appellant's App. Vol. I at 47. Therefore, the trial court held that the LDA did not create constitutionally protected contract or property rights. See Appellant's App. Vol. I at 49.

On appeal, the Court of Appeals concluded that it need not reach the issue of Section 302's constitutionality because the City "*always* retained the authority to modify" the LDAs, "regardless of Section 302." *Foundations of East Chicago v. City of East Chicago*, 905 N.E.2d 30, 35 (Ind. Ct. App. 2009) ("*East Chicago III*").

7. While these state court cases have been pending, the Attorney General has also been pursuing the civil RICO case on behalf of the City of East Chicago in federal court. *See* Appellant's App. Vol. XII at 2419. Prior to 2009, the Attorney General reached settlements with 14 defendants, including 7 individuals and 7 companies, totaling \$1,278,025 in payments. *State ex rel. Zoeller v. Pastrick, et al.*, No. 3:04-cv-0506-JM, Docket Entry Nos. 313-14, 373, 394-95, 481, 483, 484-86, 489, 493-94, 497 (N.D. Ind. filed Aug. 3, 2004). The Attorney General also achieved default judgments against A&A Enterprises; Ace Enterprise; B&S Construction; D/S Commercial Equipment & Construction; H&Y Maintenance Co., Inc.; Residential Construction Service, Inc. a/k/a Residential Roofing & Concrete, Inc. (as to liability only); and Windstorm Enterprises, Inc. *Id.*, Docket Entry Nos. 409-415.

In 2009, with a May trial date looming, the federal RICO case really began to pick up steam. The Attorney General settled with defendants Calumet Concrete and Masonry, Inc. and Timothy Raykovich on May 15 and 26, respectively. *Id.*, Docket Entry Nos. 542, 547. The liability phase of the case culminated on June 1, 2009, when the district court entered judgment on all claims—including state and federal racketeering—that the Attorney General alleged against the remaining three defendants, former Mayor Robert Pastrick, former City Councilman Frank

Kollintzas, and Pastrick's former Special Assistant James Harold Fife, III. *Id.*, Docket Entry No. 559-61.

The district court held a remedies hearing in the case on June 9, 2009, where the Attorney General requested, among other things, that the court order a forensic accounting of all casino gambling revenues paid and spent pursuant to the East Chicago LDA. *Id.*, Docket Entry No. 567. On June 22, 2009, the parties submitted proposed findings and conclusions. The Attorney General's submission to the district court includes the following two proposed rulings concerning casino gambling revenues funneled to FEC and Second Century:

6. The Plaintiffs, through the Indiana Attorney General, shall arrange for a forensic accounting to be completed within one hundred and twenty days of all money received by the foundations and Second Century during the period from 1996 through the present. Upon review of the accounting, the Court shall determine what, if any, further relief is appropriate, including restitution, disgorgement and, divestment, or otherwise, to recover funds wrongfully paid or diverted to members of the racketeering enterprise or other private parties.

7. All letters or agreements made during the administration of Pastrick relating to the allocation or disbursement of funds from the casino are hereby declared null and void. The City and the casino shall immediately confer and determine by agreement how future revenues or fees from the casino shall be allocated and disbursed. Said agreement shall be subject to the approval of the Indiana Gaming Commission to ensure that said agreement maintains the integrity of the Indiana gaming industry and serves the public interest of the citizens of the City of East Chicago and the State of Indiana.

Id., Docket Entry No. 570.

ARGUMENT

It is within this overall context that FEC urges the Court to grant review and consolidate this case with *East Chicago I* because the basis for the Court of Appeals' decision, specifically the power of the City of East Chicago to cancel its Local Development Agreement ("LDA") prior to the enactment of Section 302, is at issue in *East Chicago I*. In that case the Attorney General argued as *amicus curiae* in the Court of Appeals that an agreement diverting casino revenues intended for economic development to an unaccountable, private, for-profit corporation, is void as against public policy, *City of East Chicago v. East Chicago Second Century, Inc.*, 878 N.E.2d 358 (Ind. Ct. App. 2007), *trans. granted*, 898 N.E.2d 1219 (Ind. 2008) ("*East Chicago I*"). Also in the Court of Appeals in *East Chicago I*, the IGC, with the consent of the Attorney General, filed a brief as *amicus curiae* arguing only that the petition for judicial review challenging Resolution 2006-58 should not have been consolidated with the rest of that case. *See* Appellee's Brief of the Indiana Gaming Commission Regarding Consolidation, *East Chicago I*, 878 N.E.2d at 358. No state agency took any broader position in that case on the enforceability of the East Chicago LDA.

In light of (1) the limited role the State and its agencies have played in *East Chicago I* up to this point, (2) the Attorney General's pending constructive trust claims against Second Century, (3) the forthcoming decision of the federal district court concerning remedies in the RICO lawsuit, and (4) the need to promote judicial economy, the Attorney General has concluded, after weighing and considering all

potential State interests at stake, that a limited State response to the Petition to Transfer and Motion to Consolidate in this case is appropriate. Accordingly, the State respectfully submits that this Court should deny the Motion to Consolidate and hold the Petition to Transfer in abeyance pending resolution of *East Chicago I*. Once the Court decides *East Chicago I*, it should do one of the following with respect to this case: (1) deny the Petition outright; (2) grant the Petition and remand the case to the Court of Appeals for further consideration in light of that decision; or (3) call for further briefing from the parties so that they may appropriately address both the significance of *East Chicago I*, if any, for this case, and the significance, if any, of any remedies ordered by Judge Moody in the federal RICO case.

This route offers the virtue of permitting the Court to avoid taking the unnecessary step of determining the extent to which this case and *East Chicago I* actually overlap. In this regard, it is important to bear in mind that both *East Chicago I* and this case include multiple issues, and that *East Chicago I* is before this Court at an interlocutory stage. *East Chicago I* focuses on the extent to which LDAs are enforceable as a matter of contract law, whether Second Century and FEC are third-party beneficiaries to the East Chicago LDA, whether the City brought its claims challenging the validity of the LDA within the applicable limitations period, whether Pastrick breached his fiduciary duty to the City and whether the contract action should have been consolidated with a related, but separate, administrative action. *East Chicago I*, 878 N.E.2d at 368. Furthermore, the Court's decision in *East Chicago I* may not resolve all issues in the case, and

may leave for further litigation the same issues that FEC alleges overlap with this case (concerning East Chicago's ability to modify or cancel the LDA). *See* Appellant Foundations' Pet. to Transfer at 4-6.

Meanwhile, FEC brought this case to address the constitutionality of Section 302, a statute that arose after, and in part because of, the circumstances at issue in *East Chicago I*. It includes not only constitutional issues, but also challenges to FEC's standing to bring the case at all. *East Chicago III*, 905 N.E.2d at 36-40 (Brown, J., concurring). Only now, following the decision of the Court of Appeals, does it include an issue that potentially overlaps with *East Chicago I*.

With lack of complete overlap between the cases, and lack of certainty that the Court's decision in *East Chicago I* will finally resolve any overlapping issues, it is far from obvious that the Court should consider this case in tandem with *East Chicago I*. Accordingly, deciding the extent of that overlap, and its significance for this case, is better left until after the Court decides *East Chicago I*. At that point, depending on the nature of its decision in *East Chicago I*, and depending on what is happening with the federal RICO case pending before Judge Moody, the Court may determine that either outright denial of the Petition or remand to the Court of Appeals is the appropriate course of action.

If necessary, the Court of Appeals can assess the degree of overlap, and that decision might yield greater insight concerning the rationale supporting its original decision. Or, again depending on what this Court holds in *East Chicago I*, remand might give the Court of Appeals the opportunity to dispose of the case on other non-

constitutional grounds, such as FEC's standing, or at least to address FEC's constitutional issues in the first instance. Finally, even if the Court concludes that it must decide all issues in this case rather than deny the Petition or remand the case, its judgment would be aided by further briefing from the parties as to the significance of *East Chicago I*. Under any of these scenarios, if the Court waits to act on the Petition until after it decides *East Chicago I*, it will have better information for making its decision both as to transfer and the merits.

CONCLUSION

The Court should deny the Motion to Consolidate and hold the Petition to Transfer in abeyance pending its decision in *East Chicago I*.

Respectfully submitted,

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WORD COUNT CERTIFICATE

As required by Indiana Appellate Rule 44, I verify that this Combined Response of the State of Indiana to the Petition to Transfer and the Motion to Consolidate contains no more than 4,200 words, not including the Statement of the Issue.

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CERTIFICATE OF SERVICE

I hereby certify that on this 22nd day of June, 2009, a copy of the foregoing was served via First Class United States mail, postage pre-paid upon the following:

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