NATIONAL CONGRESS OF AMERICAN INDIANS

CURRENT TAX NEEDS IN INDIAN COUNTRY

The National Congress of American Indians (NCAI), along with its partners, the Affiliated Tribes of Northwest Indians (ATNI), the California Association of Tribal Governments (CATG), the United South and Eastern Tribes (USET), and the Native American Finance Officers Association (NAFOA) – collectively, the Intertribal Tax Initiative, appreciate the opportunity to share our ideas on tribal tax policy.

As you know, Indian tribal governments have a unique status in our federal system under the U.S. Constitution and numerous federal laws, treaties and federal court decisions. American Indian and Alaska Native tribes have a governmental structure, and have the power and responsibility to enact civil and criminal laws regulating the conduct and affairs of their members and reservations. Tribes operate and fund courts of law, police forces, and fire departments. Tribes provide a broad range of governmental services to their citizens, including education, transportation, public utilities, health, economic assistance, and domestic and social programs. Like the revenue of states and local governments, tribal revenues are not treated as taxable income – but as the governmental revenues of a distinct and unique sovereign government.

As such, federal tax reform is of great interest to NCAI, its partners, and our respective member tribes. This is because tax reform presents a very real opportunity to protect and enhance the many governmental functions and services provided by Indian tribes. There are many ways to include tribal governments in any upcoming tax reform. While the federal government recognizes that tribal nations are governments, tribes are frequently treated less favorably than state and local governments under our federal Tax Code. Such differential and unjust treatment typically results in tribal governments being denied federal tax exemptions and economic development incentives that state and local governments enjoy.

In restructuring the nation's Tax Code, it is critical that members of Congress clearly understand both the unique problems and challenges of Indian Country and the governmental status of Indian tribes. Thus, in expressing our views on potential areas

to improve tribal tax policy, we do so as partners in American growth and, like each of you, as elected governmental representatives of Native American people.

Tribal Tax Parity--A History of Uneven Progress

While there is no federal statutory provision that "exempts" Indian tribes from federal income tax, the IRS has consistently and correctly concluded that federally recognized tribes and their federally chartered corporations are not subject to federal income taxes.[1] With respect to tribal governments, the IRS in Revenue Ruling 67-284 based its conclusion on the fact that tribes (like states) are political bodies not subject to the income tax provisions of the Internal Revenue Code (the "Code").

However, the IRS did not treat Indian tribes like states for all purposes of the Code. Revenue Ruling 68-231 provided that tribal bonds could not be treated like state government-issued bonds because Code section 103, which exempts interest paid on state and local bonds from income taxation, did not specifically mention Indian tribes. The IRS took a similar approach to several other Code provisions that explicitly exempted state and local governments.

Recognizing that tribal governments should be treated on par with state governments, Congress passed the **Indian Tribal Governmental Tax Status Act** in 1982 to provide comparable governmental tax treatment to tribes for federal tax purposes.[2] The Tribal Governmental Tax Status Act, codified as section 7871 of the Code, provides that federally recognized tribes are treated like states with respect to the following:

- Deductibility of charitable contributions to governments for exclusively public purposes
- Deductibility of gifts and bequests for public purposes
- Exclusion of interest on tax-exempt bonds (subject to restrictions on tribal bonds discussed below)
- Exemption from certain federal excise taxes (subject to restrictions)
- Deductibility of taxes paid to tribal governments
- Private foundation excise tax rules referencing governments
- Provisions relating to accident & health plans under Section 105

[1] Four revenue rulings address the tax status of tribal governments: Rev. Rul. 67-284, 1967-2 C.B. 55; Rev. Rul. 81-295, 1981-2 C.B. 15; Rev. Rul. 94-16, 1994-1 C.B. 19; and Rev. Rul. 94-65, 1994-2 C.B. 14.
[2] Title II of Pub. L. No. 100-203, 96 Stat. 2605 (1982).

- Provisions authorizing retirement plans under Section 403(b) for educational employees

Although Code Section 7871 did not codify the basic tax immunity of tribal governments, the legislative history indicates that Congress was aware of the IRS's position in Revenue Ruling 67-284 and did not wish to alter it.

Unfortunately, the Tribal Governmental Tax Status Act did not live up to its original promise of treating tribes on par with states for federal tax purposes. For example, the provision that allowed Indian tribes to issue tax-exempt bonds was subject to many restrictions in the original 1982 Act, and more were added in 1987. Thus, Indian tribal bonds were subject to the following restrictions:

- An absolute prohibition on the issuance of private activity bonds, except for certain tribal manufacturing bonds subject to wage and employment tests that are virtually impossible for modern manufacturing facilities to meet

- Government bonds issued by tribes were required to meet the essential governmental function test (which was considered to be met only when (the project does not generate revenue?)substantially all of the proceeds were used in the exercise of an essential governmental function)

- "Essential governmental functions" for this purpose were limited to those functions "customarily performed" by state and local governments with general taxing powers (e.g., schools, roads and sewers).

The Tribal Tax Status Act also applied the "essential governmental function" test to the excise taxes from which tribes were exempted, even though state and local government exemptions were not so restricted.

In addition to imposing specific restrictions on tribes that were not applicable to states, Section 7871 failed to address many areas of the Code where special treatment is extended to states. Unfortunately, the IRS took the position that these omissions demonstrated that tribes should not be treated like states, and denied governmental status with respect to a number of different provisions, including various federal excise taxes not covered by Section 7871. See, e.g., Revenue Ruling 94-81, 1994-2 C.B. 412 ("Indian tribal governments have no inherent exemption from federal excise taxes").

NCAI Priority--Tribal Tax Parity

NCAI, its partners, and our respective member tribes, firmly believe that because Indian tribes are governments, they should generally be treated like states for all federal tax purposes. As part of a comprehensive tax reform bill, Section 7871 needs to be

broadened to treat Indian tribes like states for all tax Code purposes, except in those limited instances where a special rule for tribal governments is absolutely necessary. In most cases, a special rule will not be necessary.

A special rule is needed so tribes can continue to offer 401(k) retirement savings plans. Since Congress amended the Code in 1995 to specifically clarify that tribes, unlike state and local governments, could offer 401(k) plans, many tribes have adopted 401(k) plans as the primary vehicle for their employees. Many would now like to supplement such plans with governmental pension plans, and corrective legislation is needed to accomplish that goal. But Congress should preserve the right of tribal employers to continue to sponsor 401(k) plans as well.

Specific Instances where the Tribal Tax Parity is Urgently Needed

While we believe that tribes should be treated like states for all tax purposes (and generally should not be subject to special rules or restrictions that states and local governments do not have to meet), there are several specific areas where tribal tax parity is urgently and particularly needed:

- Tax Exempt Bonds (including private activity bonds)
- Employee Benefit and Pension Plan
- Tribally Funded and Controlled Charities
- Treatment as States for purposes of federal streamlined sales tax legislation

Treating tribes like states in these four areas would be a significant step forward, and should be taken in the context of comprehensive tax reform.

Tribal issuance of tax exempt bonds

A provision championed by the Senate Finance Committee in the American Recovery and Reinvestment Act (ARRA) authorized $2 billion in bond authority for a new category of bonds for Indian tribes, known as "Tribal Economic Development ("TED") Bonds." TED Bonds were intended to provide tribes with more flexibility to use tax-exempt financing than is allowable under the current "essential governmental function" standards as noted above. The TED Bond rules are still subject to other restrictions that require financed projects to be located on Indian reservations and that prohibit the financing of gaming facilities.

The ARRA provision required Treasury to conduct a study of the effectiveness of the new bonding authority, and to recommend to Congress whether it should "eliminate or

otherwise modify" the essential governmental function standard for Indian tribal bond financing. That Treasury study is now complete and was delivered to Congress on December 19, 2011.

The core recommendation of the Treasury study is that Congress should adopt the same standard for tribal government bonds as applies to governmental bonds issued by State and local governments. The Treasury Department clearly recommends repealing the "essential governmental function" standard for Indian tribal governmental bond financing. The Treasury study explains that it is making this recommendation "[f]or reasons of tax parity, fairness, flexibility, and administrability . . . ."

Treasury also recommends that Congress adopt what it calls a "comparable" private activity bond standard so that Indian tribal governments could issue some private activity bonds. Such bonds would be subject to a national volume cap, and Treasury would be authorized to make allocations among Indian tribal governments.

Treasury has further recommended that Congress limit Indian tribal bond issuances in two respects: (1) No bonds could be used for gaming projects, and (2) some kind of project location restriction would apply. With respect to the latter, Treasury has recommended that Congress provide more flexibility than it did for the TED Bonds under ARRA. Specifically, Treasury recommends that tribal bonds be allowed to finance projects that are located on Indian reservations, together with projects that both: (1) are contiguous to, within reasonable proximity of, or have a substantial connection to an Indian reservation; and (2) provide goods or services to resident populations of Indian reservations.

NCAI, its partners, and our members appreciate the analysis and core recommendations in the Treasury study, but have serious concerns about the "project location restriction"--even in its modified form. In particular, the requirement that the financed project provide "goods or services" to reservation residents would effectively kill the chances of using tax-exempt debt for many tribal economic development projects. This directly infringes on tribes' ability to diversify their economic revenue generating base. The requirement for proximity to an Indian reservation would eliminate a tribe's ability to meet state-wide government contracting requirements. It is our view that tribal governmental bonds--as distinguished from private activity bonds--should not be subject to a "project location" restriction of any type. The Congress must remember that tribal governments do not have the typical taxing base of state and local governments and their business revenues are the core revenue base that enables tribes to become less dependent on federal resources.

Tribal pension and employee benefit plans

If the "essential governmental test" is unworkable in the government bond context, it is proving to be even more unworkable in the tribal employer plan arena.

DOCKET ALARM

Explore Litigation Insights

Docket Alarm provides insights to develop a more informed litigation strategy and the peace of mind of knowing you're on top of things.

Real-Time Litigation Alerts

Keep your litigation team up-to-date with **real-time alerts** and advanced team management tools built for the enterprise, all while greatly reducing PACER spend.

Our comprehensive service means we can handle Federal, State, and Administrative courts across the country.

Advanced Docket Research

With over 230 million records, Docket Alarm's cloud-native docket research platform finds what other services can't. Coverage includes Federal, State, plus PTAB, TTAB, ITC and NLRB decisions, all in one place.

Identify arguments that have been successful in the past with full text, pinpoint searching. Link to case law cited within any court document via Fastcase.

Analytics At Your Fingertips

Learn what happened the last time a particular judge, opposing counsel or company faced cases similar to yours.

Advanced out-of-the-box PTAB and TTAB analytics are always at your fingertips.

API

Docket Alarm offers a powerful API (application programming interface) to developers that want to integrate case filings into their apps.

LAW FIRMS
Build custom dashboards for your attorneys and clients with live data direct from the court.

Automate many repetitive legal tasks like conflict checks, document management, and marketing.

FINANCIAL INSTITUTIONS
Litigation and bankruptcy checks for companies and debtors.

E-DISCOVERY AND LEGAL VENDORS
Sync your system to PACER to automate legal marketing.