

NAFOA Written Testimony
Select Revenue Measures Subcommittee
Examining the Impact of the Tax Code on Native American Tribes
March 4, 2020

NAFOA's mission is to strengthen tribal finance and grow tribal government economies by building best practices, creating beneficial partnerships, and advocating for effective policy solutions. We are honored to represent the economic interests of over one hundred-twenty tribal governments, and consider it a privilege to offer our comments on necessary tribal tax reform to the Ways & Means Committee. Improving the current tax code to provide parity with other governments and improving access to federal capital programs will significantly impact tribal economies for the better and enhance the current welfare of Indian Country.

Tribal governments have come to view revenues derived from economic development as a necessity to supplement or fully fund vital programs and services. This tribal government reliance on economic growth and development has made Congress and the Administration's role in promoting growth and development much more important as well. A role that is an obligation to protect and enhance tribal self-governance, and one that the federal government must work to fulfill.

Overview of Federal Trust Responsibilities

Treaties signed between tribes and the federal government, judicial decisions, Executive Orders, laws, and statutes have determined that the federal government has a legal trust obligation to tribes. This trust obligation has been defined as the federal government's responsibility to protect Indian trust lands, Indian rights to use and access those lands; to provide basic social, education, and medical services to benefit the general welfare of the tribe; and to uphold tribal sovereignty and self-governance.

Tribal governments, similar to state governments, have the authority and responsibility to develop infrastructure and oversee services that would benefit their citizens. However, tribal governments face additional obstacles in funding these responsibilities. Tribal governments have added restrictions placed on existing federal programs that are designed to assist in infrastructure and economic development.

Federal policy must follow a framework that acknowledges the federal government's obligation to support tribal governments in their efforts to promote economic prosperity. Overall, federal policies and programs aimed at improving the quality of life in America have woefully left Indian Country out of the equation thus violating trust obligations. As a result of the failure to uphold federal obligation, tribal governments have long been passed over in numerous tax provisions and economic incentives.

Access to Capital: Tax Credits

Tribal governments are in some of the most economically distressed and disadvantaged areas in the country with high levels of generational poverty and unemployment. Tribal governments are on federal trust lands making property taxes, which most governments rely upon, unusable for tribal governments. The lack of a property tax base means that tribal governments rely on revenue from their business enterprises to provide government services. Reliance on revenue makes incentives and programs that promote private investment, like tax credits, even more valuable for Indian Country.

Tax credits serve an important role for tribal governments since tribal governments can only issue debt and tax credits act like an equity investment for a portion of a project. Because of the equity-like credits, the New Markets Tax Credit, Low Income Housing Credits, and Indian Employment could potentially provide the greatest benefit to tribes wishing to build community facilities, grow their local economies, and create jobs.

Tribal governments face multiple obstacles to providing government services such as public safety, education, housing, healthcare, and cultural programs. First, tribal governments lack access to capital and tax incentives meant attract investors and businesses to Indian Country. This lack of effective access to capital is prevalent in tribal governments in early stages of economic growth that need flexible and initial seed capital and in tribal governments in advanced stages of growth that need significant amounts of cost-effective capital to fund multifaceted projects.

For decades, tribes have been advocating for legislation that removes the barriers to utilizing tax credits and accessing capital. The federal government's responsibility to tribes mandates prioritizing legislative fixes for the New Markets Tax Credit, Low Income Housing Tax Credit, and Indian Employment tax programs so that tribal economies can thrive.

New Markets Tax Credit (NMTC):

In 2000, Congress established the New Markets Tax Credit Program to spur investments into projects located in low-income communities. The program provides needed capital and credit in areas that have little or no banking access. The Community Development Financial Institutions (CDFI) Fund allocates tax credit authority to Community Development Entities (CDEs). CDEs can offer tax credits to investors who make Qualified Equity Investments (QEIs) to CDEs, and CDEs can provide better rates and terms on loans to businesses in low-income communities. Since the NMTC inception, the CDFI has delivered \$70 billion in tax credit authority which then created 750,000 jobs and financed health and community centers, commercial, and industrial facilities¹.

Despite the NMTC's substantial distribution of tax credits, tribal communities and tribally focused CDEs have been left behind with, on average, less than one half of one percent of the NMTC allocations going to Indian Country in the years prior to 2017. Since 2017, the Department of Treasury placed an emphasis on allocations serving Indian Country by placing a box on the application that applicants check if their projects are serving Indian Country. Most applicants check the box if their projects are close to a tribe in the hopes of receiving greater consideration. While this may have helped emphasize the need for tribal allocations and had the effect of increased tribal projects, it has led to confusion over the actual number of tribal projects that were actually funded. Allocations to Indian Country still remain far below comparable expectations and need. The current application process and a broad unfamiliarity of how to serve and navigate the unique needs of Indian Country has effectively left out tribal communities who often have the greatest need for capital and credit.

Congress should direct the Treasury to issue regulations that provide for the Community Development Financial Institutions Fund to allocate, on aggregate, NMTCs to CDEs that intend to use the cash from a QEIs to make qualified low-income community investments in proportion to the U.S. population of Native Americans. To ensure that the credits are reaching Indian Country, Congress should amend the definition of low-income community to improve direct tribal community access to NMTC dollars.

¹ Community Development Financial Institutions Fund, "Community revitalization by rewarding private investment," 2018, https://www.cdfifund.gov/Documents/NMTC%20Fact%20Sheet_Jan2018.pdf

Low Income Housing Tax Credit:

Indian Country faces more severe rates of overcrowding, physical housing problems, and unaffordable housing than any other population in America. While many factors contribute to and complicate this housing crisis, financing for affordable housing in Native communities is a serious concern. According to a Department of Housing and Urban Development (HUD) report, American Indian and Alaska Native households were more likely to experience financial burden than non-American Indian/Alaska Native households, with more than 50 percent of household income going towards housing costs².

The Low-Income Housing Tax Credit was established in 1986 to create greater incentives for the private market to invest in affordable rental housing. Federal tax credits are awarded to developers of affordable housing projects. Developers can sell these credits to investors to raise capital and equity for their projects. However, tax credits are allocated to state-agencies and are based on population, as opposed to need. This prioritization, and lack of regulation requirements, leaves no incentive for states to consider tribal housing projects in their IRS approved Qualified Allocation Plans. As it stands, this funding pass-through is not working for tribal governments.

In addition to the lack of incentive for states to include tribal governments, there is a lack of an incentive for capital to fund housing projects on tribal lands. The challenge of developing on trust lands under tribal laws in coordination with HUD regulations specific to tribal housing authorities makes an incentive necessary.

Congress should fix the current housing tax credit allocation by including a process for tribal governments to directly receive consideration for funding for housing tax credits and move tribes into the Difficult Development Area status. This fix will provide greater certainty and increased funding for needed housing in Indian Country.

Indian Employment Tax Credit:

Indian Country has experienced severe unemployment rates much like the rates seen during the Depression Era for generations. Unemployment rates in Indian Country that, until more recently,

² U.S. Department of Housing and Urban Development, "Continuity and Change: Demographic, Socioeconomic, and Housing Conditions of American Indians and Alaska Natives," 2014, https://www.huduser.gov/portal/publications/pdf/housing_conditions.pdf

averaged over 20% - the highest unemployment in the country. While the overall rate had decreased more recently, some tribes are still experiencing unemployment beyond depression-era rates.

A potential solution to decrease unemployment is the Indian Employment Tax Credit. The Indian Employment Tax Credit provides private businesses an incentive to hire enrolled tribal members and their spouses who live on or near an Indian reservation. Employers operating on an Indian reservation can receive up to 20 percent income tax credit for the first \$20,000 of qualified wages and qualified employee health insurance costs. The credit benefits both the community and the business by creating an incentive to hire tribal members, diversifying the workforce, and reduces the overall tax liability for the business. However, the current formula is administratively burdensome, and the credit amount is outdated which deters businesses from utilizing this credit.

In order to increase utilization of this credit, Congress should modify the tax credit formula to the average of qualified wages and health insurance costs from the last two tax years. The wage amount should be updated to \$30,000 in qualifying wages and health insurance costs per eligible employee and the “high wage jobs” maximum should be raised from \$45,000 to \$60,000.

Access to Capital: Financing

Tax-Exempt Debt

Over three decades ago, Congress recognized the need for tribal governments to issue tax exempt debt for government services and development when they authorized its use by tribes. While tribal governments were authorized to issue debt, they were prevented from using it fully due to the strict limitations of an “essential governmental function” test. While state governments receive financing for projects such as housing, recreational facilities, and tourism activities, tribal governments are denied funding for the same projects because the interpretation of the current code deems these projects as “non-essential.” The irony of tribal governments only issuing general obligation bonds that are typically repaid using property and other taxes that tribal governments can’t support since they are on trust lands or don’t have the population, while being shut out of “non-essential” revenue or private activity bonds that they can support has not been lost on tribes.

To partially remedy this lack of equity, Congress created the two-billion-dollar Tribal Economic Development Bond or TEDBs program in 2009. This program recognized tribal authority to issue tax-

exempt debt for a broader scope of activities including economic and enhanced community development. The partial fix made it easier for tribes to utilize tax-exempt debt, however; this program is a temporary fix and funding has run out making it imperative that Congress act.

Parity between tribal and state governments should be acknowledged by eliminating the “essential governmental function,” test of the tax code. We cannot continue to use an inequitable practice against the development activities of tribal governments. Removing this test will give tribes equal access to the tax-exempt bond market on equal terms as state and local governments.

Governmental Parity

Improving the federal tax code to provide greater access for credit programs and financing is important for tribal development. However, it is also important to fix the tax code to provide parity in governmental services that inadvertently place tribes at a disadvantage in their application. This includes Indian adoptions, child services, and the ability to establish charities for public services.

Tribal Foundations and Charities

A 501(c)(3) can be classified, either as a public charity or a private foundation. Public charities receive advantages over private foundations. Charities have higher donor tax-deductible giving limits, can receive support from other public charities and private foundations, and have less complex 990 tax returns. Charities funded and organized by tribal governments do not receive the same public charity designation that other government-controlled charities are given. Tribal governments can only be private foundations and are subjected to restricted regulations and higher compliance costs than public charities. Support from state and local governments are treated as "public support" while support from a tribal government is not treated as support from a governmental entity. Organizations formed to support state and local governments are treated as "supporting organizations." However, the status of organizations formed to support tribal governments is unclear. What is clear is that the lack of parity between tribal and other tribes prevent tribes from forming and funding separate 501(c)(3) nonprofit organizations, and thus prevents tribal charities from ever truly thriving.

Congress should amend Section 170(b)(1)(A)(vi) to treat charitable organizations formed to support tribal governments the same as organizations formed to support state and local governments.

Tribal General Welfare Programs Clarification

Tribal governments have been taking care of elders and youth for centuries. The General Welfare Exclusion (GWE) Act acknowledges the cultural values tribes place on community wellness, and exempts tribal government programs, services, and benefits for tribal citizens, their spouses, and dependents from income under the Internal Revenue Code. However, the Social Security Administration does not exclude GWE benefits from income eligibility for supplemental security income benefits. Disabled and elderly tribal citizens receiving GWE benefits have experienced reduced federal benefits and in some cases are deemed ineligible. These tribal services improve the welfare of their citizens and should be excluded from consideration in federal benefit formulas.

Congress should clarify that a GWE benefit provided by a tribal government pursuant to the Tribal General Welfare Exclusion Act (26 U.S.C. § 139E) is excluded from consideration for purposes of determining the recipient's eligibility to receive supplemental security and disability income benefits (42 U.S.C. § 1381 et seq). This is entirely consistent with the intent of the Act.

Adoption Credit

The adoption credit was created to reduce the number of children waiting for adoption and is meant to help lessen the financial burden of adoptions. According to a 2016 study³, 84 percent of the nearly 57,000 children adopted through public agencies were designated as having “special needs.” Parents that adopt a “special needs” child can claim the maximum credit of \$14,080. However, the current tax law only allows states to designate a child as “special-needs.” Because tribes have jurisdiction over child welfare, Native children cannot be designated as “special-needs” and parents are unable to claim this adoption credit and must bear an unfair financial burden.

To relieve this burden, amend the Internal Revenue Code (IRC) § 7871(a) to refer to IRC § 23, so tribes can designate a Native American child as “special-needs,” allowing parents to claim the adoption tax credit. Native children deserve to grow up in loving households and should have the same opportunities to leave the foster care system as children within state welfare agencies. Making this adoption credit available for

³ See Children’s Bureau, U.S. Dep’t of Health & Human Services, The AFCARS Report: Preliminary FY 2016 (2016) available at https://www.acf.hhs.gov/sites/default/files/cb/special_needs2012_2016.pdf.

Native children will help to expediate the adoption process and will decrease the number of Native children waiting for adoption.

Child Support Enforcement

Child Support Enforcement (CSE) agencies oversee the cash transfer from the non-custodial parent to the custodial parent for the financial support of his or her children. Tribal CSEs operate just as state agencies in enforcing child support orders. Unlike states, tribal CSEs cannot access the Federal Income Tax Refund Offset Program that uses a portion or all a non-custodial parent's expected refund to pay delinquent child support. Presently, tribal agencies can only utilize income withholding enforcement mechanism. This limitation impedes the ability of tribal CSE programs to administer their services, and child support can remain uncollected. Children's welfare is detrimentally impacted when households no longer receive steady financial support. Access to the Tax Refund Offset will ensure that Native children will not have to face the risks associated with financial insecurity.

For tribal CSEs to effectively operate, Congress must amend Section 455(f) of Title IV-D to permit Indian tribes or tribal organizations receiving funding under as CSE agencies to participate in the Federal Income Tax Refund Offset Program.

Conclusion

Tribal governments have long been passed over in numerous tax provisions and economic incentives that could boost Indian Country economies. Even when Indian Country is taken into consideration for the development of various regulations and progress, Indian Country continues to be omitted from economic advancement due to the lack of parity between tribal governments and state or local governments and the multitude of barriers that prevent tribes from accessing capital and tax credits. Congress can exercise its obligation to maintain the general welfare of tribes and continue to support their trust responsibility by fixing inadequate codes and regulations. NAFOA highly encourages the Ways & Means Committee to consider these recommendations and realize the substantial impacts these changes will create.