

**Written Testimony of Chairman Kenneth Kahn
Santa Ynez Band of Chumash Indians
To the House Ways & Means Committee Subcommittee on Select Revenue
Measures
March 4, 2020**

Chairman Thompson, Ranking Member Smith, Members of the Committee, thank you for inviting tribal leaders to testify before you today. It is an honor to be here on behalf of the Santa Ynez Band of Chumash Indians, where I serve as elected chairman, and to advocate for tax reform on behalf of tribal governments across the country.

A common theme you will hear today is the need to ensure tax parity for tribal governments with state and municipal governments, all of which share the common goal of generating economic activity to support services and employment for their citizens.

Tribal governments have long faced difficulty in securing reliable financing, and because they lack tax revenues, it is generally only those tribes able to leverage revenues from natural resources, energy, or gaming which have been able to secure substantial financing. Many tribes, however, do not have robust revenues with which to secure financing, and most are located in remote areas with few economic opportunities.

Despite these challenges inherent to tribal governments, we also lack a key tool available to state and municipal governments: access to tax-exempt financing, which

makes projects much more attractive to investors. In fact, from 1987 through 2010, Indian tribal governments issued an average of about \$157 million annually in tax-exempt bonds for a total of about \$3.76 billion in 321 total transactions. While this would seem to be a significant amount of development, this figure represents all of Indian Country and equals less than one-tenth of one percent of the total \$6.599 trillion in new issues of long-term tax-exempt municipal bonds issued during this period.¹

What accounts for this overwhelming disparity? Unlike state and municipal governments, tribal governments are subject to the Essential Government Function test, or "EGF". The EGF was enacted originally in 1982 as part of the Indian Tribal Government Tax Status Act, a bill initially developed to address tribal tax parity issues, but ultimately limited the use of tax exempt bonds to schools, streets, or sewers, but not activities financed with private activity bonds. This area of the Code was again amended in 1987 to further limit the scope of the EGF to not include any functions which are not customarily performed by state and local governments with general taxing power². By comparison, state and local governments may use tax-exempt bonds to finance a much wider array of job-creating, revenue-generating projects, ranging from convention centers to commercial buildings.

¹ See Report and Recommendations to Congress regarding Tribal Economic Development Bond provision under Section 7871 of the I.R.C, Depart. of the Treasury, Dec. 2011

² See The Omnibus Budget Reconciliation Act of 1987, Pub. L. No. 100-203

In practical terms, this means that projects on tribal land face substantially higher financing costs than identical projects undertaken by state and municipal governments. In fact, tribal governments lack of access to tax-exempt financing increase our borrowing costs to about 25% higher than those of state and municipal governments, creating a significant disincentive to investment in tribal communities.

It is also important to note that the EGF doesn't limit the use of federal funds or other public monies, but is simply a restriction on how a tribal government may finance projects which are paid for with tribal funds.

Members of the Committee, I am here to ask that you take action to lift the restrictions the Essential Government Function test imposes on tribal governments.

Congress has already recognized the flaws of the the EGF and, in 2009, acted to temporarily address this disparity by creating the Tribal Economic Development Bond program, authorizing tribal governments to issue a combined \$2 billion in tax-exempt bonds. Eligible projects are not subject to the EGF, must be located on tribal land, may not be gaming facilities, and each allocation of tax-exempt financing must be approved by Treasury.

Implementation of the program demonstrated the strong appetite for economic development in Indian Country, as tribal governments used this opportunity to secure tax-exempt financing for projects across the nation. My tribe was approved

by Treasury to issue tax-exempt bonds to support construction of a new hotel and parking structure on our reservation, a project which has substantially improved our ability to provide services to our members.

However, the program had several shortcomings: first, the \$2 billion cap on tax-exempt bonds has already been reached, limiting use to only those tribes which had projects approved over the last decade instead of providing a valuable tool to all tribal governments.

Second, the program's initial regulations failed to recognize the realities of construction timelines and were so prescriptive that only 3% of the \$2 billion was successfully allocated in the first two years after Congress took action. While Treasury later updated its requirements, these original rules hampered the ability of many tribes with shovel-ready projects to take immediate advantage of this limited opportunity.

Finally, neither the authorizing legislation nor Treasury's regulations addressed whether bonds issued under the program maintained tax-exempt status when refinanced. This oversight threatened to upend the viability of many projects which had already been undertaken by causing significant increases in financing costs, increases which had not been considered in projects' original business plans.

Despite recognition by Treasury of what was essentially a ticking time bomb, it took years of concerted advocacy by tribal leaders to secure guidance clarifying that

tribal bonds maintain tax-exempt status when refinanced, just as virtually every other tax-exempt government bonds do.

Ultimately, despite the construction of many worthwhile projects, perhaps the primary outcome of the Tribal Economic Development Bond program was to persuade tribal leaders that we needed to seek a long-term ability to access tax-exempt financing.

It isn't just Congress which has recognized the negative impact of the EGF on tribal governments: the Treasury Department, Government Accountability Office, and Joint Committee on Taxation have all identified the EGF as an obstacle to tribal economic development.

The Treasury Department undertook a study of the EGF in 2011, ultimately recommending³ in its report to Congress that "tax policy warrants providing parity between Indian tribal governments and State and local governments for tax-exempt Governmental Bond financing eligibility purposes".

The JCT has repeatedly noted that "bonds issued by tribal governments are subject to limitations not imposed on State and local government issuers", while the GAO, in

³ "Report and Recommendations to Congress regarding Tribal Economic Development Bond provision under Section 7871 of the Internal Revenue Code", 2011, accessed at <https://www.treasury.gov/resource-center/tax-policy/Documents/Report-Tribal-Bonds-2011.pdf>

a report⁴ to the Senate Finance Committee, found that the vagueness of the EGF restriction increased the tax compliance burden on Indian tribal governments”. The GAO report also identified hundreds of stadiums, zoos, convention centers, hotels, and rental housing projects financed with tax-exempt bonds, and noted that at least 120 golf courses in 29 states had been built by local governments with tax-exempt financing.

Mister Chairman, Ranking Member, members of the committee, as you consider means to provide equal tax treatment to tribal governments, I hope that a repeal of the Essential Government Function test is a component of any resulting legislation. This antiquated restriction on tribal governments has been widely recognized as inequitable and Removal of this restriction on financing, which is applied only to tribal governments, would provide a valuable tool to attract investment in tribal communities, regardless of their location or current economic activities.

⁴ Information on Selected Capital Facilities Related to the Essential Governmental Function Test GAO-06-1082: Published: Sep 13, 2006, accessed at <https://www.gao.gov/products/gao-06-1082>