

ESTABLISHING A TRIBAL ECONOMIC DEVELOPMENT ENTITY

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HYPOTHETICALS

- *FutureEnergy Inc.*, a NV corporation, approaches the tribe with a breakthrough development that harnesses atomic energy through fusion technology they developed. The owners only need a location to locate the completely enclosed equipment that will be fully encased with metal walls. They need a lease of tribal land for 25/25 years. Guaranteed to make the tribe millions on energy sales and lease payments. They must have a binding Letter of Intent signed today. The letter prohibits the tribe from discussion of the project with any third parties and that the tribe will submit a land lease to the BIA within 30 days.
- *BlackJack Development Inc.* Company is offering to buy land approximately 400 miles from the current reservation and assist the tribe in taking the land into trust. Once in trust, the company will build the tribe a casino and resort. 70/30 split in profit for first 5 years, then 50/50 for 5 years, and then full profit to the tribe. Must sign a Development Agreement TODAY!

HYPOTHETICALS

- Cannabis development—developer guarantees \$600 million pure profit to the tribe in the first year! No problems with the U.S. Attorney's Office or local sheriff.
- Payday Lending—tribe told the venture is risk free and only needs the tribe to act as the regulatory body for the companies that will actually be operating the lending. Interstate transactions no problem. No federal regulations to worry about. Sign 300 page Agreement TODAY and no need to involve the tribal attorney as their attorneys are experts in the field and have done 100s of similar projects.
- Patent sold to tribes and re-licensed back to the original patent owner.
- Tribally owned and operated Workers' Compensation Insurance program.
- Mini-Mart that sells tax free fuel and cigarettes.

LOTS OF MONEY BUT SOMEONE COULD GO TO JAIL—DON'T LET IT BE THE TRIBE

- A Manhattan jury found auto racer Scott Tucker and his attorney Timothy Muir guilty (14 counts each) of operating a \$2 billion criminal payday loan empire that preyed on millions of vulnerable borrowers and entered into sham deals with Native American tribes in a cynical, illegal effort to evade consumer lawsuits and law enforcement.

GOALS OF THIS TRAINING

- Formation options—pros and cons:
 - Immunity considerations;
 - Tax implications.
- Evaluating proposed development projects:
 - Prevent tribes from falling prey to shady business ventures ;
 - Properly vetting and conducting due diligence.
- Proper operation and management of tribal businesses on behalf of the tribe.
- The Mesa Grande Band of Mission Indians' experience with all of the above.

FORMATION CONSIDERATIONS

- Tribal sovereign immunity;
- Tax implications;
- Financing—access to investments and grant funding;
- Costs associated with various formation options;
- Separation of tribal politics and economic development.

FORMATION OPTIONS

- Tribally created entity through Ordinance or Resolution
- Tribally chartered or certified corporation pursuant to a Tribal Corporation Ordinance or similar ordinance
- Section 17 Corporation chartered under Indian Reorganization Act (IRA)
- Organization under state law (Corporation, LLC, Joint Ventures, and Partnerships)

TRIBALLY FORMED ENTITY

- **Unincorporated tribal entity:**
- Formed through tribal resolution or ordinance;
- Considered an Agency, Division, or Instrumentality of the tribe which is carrying out economic development activities;
- May have separate governing body comprised of elected or appointed tribal members and/or members of the Tribal Council;
- Revenue from economic development is deemed tribal general funds;
- Suing the economic entity is a suit against the Tribe and barred by immunity;
- Revenue is exempt from state and federal taxes.

TRIBALLY FORMED ENTITY

▪ **Tribal Corporation:**

- Formed pursuant to a tribal Corporation Code or Ordinance;
- “Corporation” by definition is a separate entity created to generate revenue for the corporate owners or shareholders;
- Charter or Articles and By-Laws define “purpose”, delegated authority, composition of Board of Directors, level of Tribal Council control, ownership of corporate assets, removal from Board of Directors;
- Assets are generally owned by and in name of the corporation;
- Generally operates independently of the tribe in conducting businesses;
- Depending on corporate structure, may have tribal immunity if not waived in transaction;
- Exemption from federal taxes is uncertain.

FORMATION IMPACTS TRIBAL IMMUNITY

- Sovereign immunity is critical in forming the tribe's economic development entity, under any option;
- Immunity arises in two scenarios:
 - When sued by an employee or some person associated with entity;
 - When sued by the person or entity the tribe is engaged with in business.

IS THE ENTITY AN “ARM OF THE TRIBE”?

- Test to determine if a tribally created entity is an “arm of the tribe” and can invoke immunity:
 - How was the entity created or formed (tribal, federal, or state law);
 - The purpose of the entity (commercial or government purpose);
 - The entity’s structure, ownership, and management, including the amount of control the tribe has over the entity;
 - Whether the tribe intended the entity to have tribal immunity;
 - The financial relationship between the tribe and the entity (can the entity bind tribal assets or obligate tribal assets, will a judgement against the entity reach tribal assets); and
 - Whether the purpose of tribal immunity is served by granting immunity to the entity.

IS THE ENTITY AN “ARM OF THE TRIBE”?

- Applying the test:
- ***Cook et al. v. Avi Casino Enterprises, Inc.***, 548 F 3d 718 (9th Cir. 2008) (involved injury to person from vehicle accident caused by casino employee)
- Formation: Avi Casino Enterprises (ACE) was a tribally chartered corporation under tribe’s Business Corporation Ordinance;
- Purpose: Generate income to support tribal programs and the welfare of the tribe;
- Structure, ownership, management and control by the tribe: ACE is wholly owned and controlled by the tribe, shareholder functions are performed by the Tribal Council on behalf of for the benefit of the tribe, majority of ACE’s Board of Directors are required to be tribal members;

IS THE ENTITY AN “ARM OF THE TRIBE”?

- Financial relationship between the tribe and the entity: All surplus funds from the casino not used for corporate development must be deposited in the tribe’s general fund;
- Did the tribe intend for the entity to have tribal immunity: Not discussed but clear that the tribe would want to preserve ACE’s assets since they support government programs and further economic development ;
- Whether the purpose of tribal immunity is served by granting immunity to the entity: Not discussed but immunity preserves tribal self-determination and protects the tribal treasury, one of the main purposes of tribal immunity.
- ACE was found to be “arm of the tribe” and entitled to tribal immunity from suit.

LESSONS ON IMMUNITY LEARNED FROM CASE LAW

- Entities being created by and under tribal law is a strong factor weighing in favor of immunity;
- Purpose of the entity is to generate revenue for the tribe to fund and carry out tribal programs (housing, employment for members, supporting community safety programs,...) and well being of the tribe;
- Tribal members have some role in the entity's management either on the Board of Directors or actively involved in business operations. Entity reports to tribe on business activities and accounts to tribe on financial state of tribal enterprises;
- Revenue generated by businesses operated by the entity flows to the tribe's general fund--not all of it but some of it;
- **Clearly State in Formation Document:** Intention to have entity covered by immunity. Immunity is needed to protect tribal revenue that supports the tribe's general welfare. Granting of immunity will foster tribal self-determination by generating income for tribes to become self-sufficient.

FORMATION AND FEDERAL TAX EXEMPTION

Unincorporated Tribal Entities:

The IRS generally treats unincorporated tribal entities as extensions of the tribe and therefore exempt from federal tax (Tribal Governmental Tax Status Act , IRS 7871);

Tribal Corporations:

The IRS has no formal rule or legal position on tax treatment of tribally chartered corporation, since a corporation is by definition a separate entity;

The IRS instead, like the courts, has developed a multi-factored test to determine whether the entity/corporation is a “integral part” of the tribe and thus exempt from federal taxation.

IRS TEST FOR “INTEGRAL PART”

- Whether the tribal government has the authority to terminate the corporation/entity;
- Whether the tribal government or members of the tribe elect members to the corporation's/entity's board;
- Whether the tribal government has the power to recall or remove the members of the corporation's/entity's board;
- Whether the tribal government has made a substantial financial commitment (or transferred significant property) to the corporation/entity;

IRS TEST FOR “INTEGRAL PART”

- Whether the tribal government has a substantial right to the profit earned by the corporation/entity;
- Whether the tribal government is liable for the acts of the corporation/entity; and
- Whether the corporation/entity is essentially an operating unit or agency of the tribal government.

IRS PRIVATE LETTER RULING ON TRIBAL CORPORATION AND TAX STATUS

- IRS will consider all of the facts and circumstances, including the tribe's degree of control over the enterprise and the tribe's financial commitment to the enterprise.
- **Case example -- IRS found tribally created corporation (Authority) exempt:**
- "Authority's board of directors serves at the pleasure of the tribal legislature. The legislature appoints all nine members of the board of directors. Six of the appointed directors are required to be members of the tribal legislature. The tribal legislature created Authority for the purpose of managing a tribal business on tribally owned property. The tribal legislature is empowered by the tribal constitution to enact uniform rules to govern tribal businesses such as Authority. Finally, the tribal legislature has the power to terminate Authority's charter."

IRS PRIVATE LETTER RULING ON TRIBAL CORPORATION AND TAX STATUS

- **Case example continued:** “The financial commitment Tribe has made to Authority is also substantial. Tribe will purchase the land to be used for the gaming enterprise. Tribe will hold the sole proprietary interest in the gaming activities. Profits from the gaming business are turned over to the Tribe by Authority every month. Authority must provide regular financial reports to Tribe. Authority's accounting system was set up by and its annual audits are carried out by an independent accounting firm chosen by Tribe.”

PROS OF TRIBALLY CREATED CORPORATION OVER UNINCORPORATED ENTITY

- Pros ---

- Removes politics from interfering with economic development—the entity does not change with each and every election cycle;
- 3rd parties more familiar with and often more comfortable with dealing with an independent entity than a political body such as Tribal Council;
- Frees the Tribal Council and administration to focus on governmental functions and not become consumed with tribal businesses;
- Allows greater flexibility on who can be a member of the entity's Board of Directors, e.g. may include non-Indians with business expertise;
- Allows for more efficient and effective business dealings and operations, e.g. the entity's Board can make timely decisions without having to convene a Tribal or General Council meeting to get approval on a contract or agreement;
- Easier to obtain conventional financing.

CONS OF TRIBALLY CREATED CORPORATION OVER UNINCORPORATED ENTITY

- Cons-----

- Less tribal control can mean greater risk of corruption;
- Uncertainty of federal tax exemption (“integral part” test);
- Immunity may be harder to invoke because the corporation is a separate entity from the Tribe;
- More difficult to dissolve -- a process needs to be followed for dissolution;
- Can create power struggles and turf wars between the Board of Directors and Tribal Council;
- Subject to greater General Council distrust and conflict.

CORRUPTION CAN HAPPEN

- The Chippewa Cree Tribe created the Chippewa Cree Construction Corp. — a tribally owned and federally chartered corporation — the company received more than \$33 million in federal funding, to build a water system. Tony J. Belcourt, Chippewa Cree Construction's CEO and contracting officer awarded a sole-source, no-bid contract of \$500,000 to a consulting company after receiving \$163,000 in bribes in exchange for the contract.

SECTION 17 FEDERALLY CHARTERED CORPORATIONS

- Under Section 17 of the IRA, a tribe may charter itself or other tribal entity as a corporation to conduct economic development activities for the tribe;
- Tribe does not have to be an IRA tribe to have a Section 17 corporation;
- The Corporate Charter (standard form) must be approved by the BIA;
- The Charter provides for the purpose of the corporation, duties and responsibilities, and delegated authority, including the power to grant a limited waiver of immunity.

SECTION 17 FEDERALLY CHARTERED CORPORATIONS

- Powers generally granted:
 - To buy and sell real and personal property, including to purchase fee lands;
 - To enter into leases or mortgages of tribal lands for term of 25 years without BIA approval;
 - To enter into contracts or agreements without BIA approval;
 - Further powers “as necessary to the conduct of corporate business.”
- The Board of Directors is appointed by the tribe but the Board has direct control over the business activities of the corporation;
- The Tribal Council is not involved in the day-to-day activities of the corporation, but sets strategic economic policies .

SECTION 17 FEDERALLY CHARTERED CORPORATIONS -IMMUNITY

- Without a waiver provision in the Charter, the corporation is immune from suit;
- However, waiver authority is necessary if the corporation is going to do business in the outside world;
- Waiver language is generally limited to business claims and transactions, the property that is subject to execution of any judgement and the class of persons who may sue;
- Corporate assets are owned by the corporation and held in the corporate name;
- If sued the judgment may only be satisfied with corporate assets and not tribal funds or property.

SAMPLE WAIVER LANGUAGE

- *To sue or, as further provided in this Article VIII.B, be sued in its corporate name. In granting the Board this power to be sued, the Tribe does not intend to waive [NAME OF CORPORATION] sovereign immunity from suit. Rather, the Tribe hereby authorizes the Board of Directors, and no other corporate officer, employee or agent, to authorize waivers of the Corporation's sovereign immunity as set out herein. Waivers of the Corporation's sovereign immunity from suit must be considered by the Board on a transaction by transaction basis. Such waivers shall be limited to the extent of assets specifically pledged by the Board for that transaction. In order to waive the Corporation's sovereign immunity, the Board must take official action on each proposed waiver and by resolution set the conditions, terms, and limits of the Corporation's waiver of immunity for that transaction. Nothing in this Charter shall be construed, interpreted or implied to have waived the sovereign immunity of the Corporation except as explicitly set out above.*

SECTION 17 FEDERALLY CHARTERED CORPORATIONS –TAX EXEMPT

- Section 17 corporations are exempt from federal taxation!
Revenue Ruling 81-295 and 94-16
- Regardless of whether the corporation is operating on or off the reservation.

STATE INCORPORATION

- Formation is relatively easy under state law;
- Tribally formed entities and Section 17 corporations do not lend themselves to ownership by multiple owners—state formation options do;
- May still claim immunity but is a little harder and depends on what federal circuit the entity is in---the law is divided (non-profit v. for profit, on reservation or off);
- May still have federal tax immunity depending the nature of the entity and state formation—tribe becoming a member of an existing LLC can claim federal tax exemption for its portion of the LLC income;
- Downside is entity will be subject state corporation or other state entity regulation.

STATE INCORPORATED TRIBAL LLC – IS THE ENTITY AN “ARM OF THE TRIBE”?

- Case where the court found that the tribal LLC incorporated under state law was not “arm of the tribe”:
- *American Property Management Corp. v. Superior Court of San Diego*, 2012 (breach of plaintiff’s management contract with U.S. Grant Hotel Ventures)
- Formation: Sycuan Tribe chartered Sycuan Tribal Development Corporation (STDC) under tribal law. STDC invested in the purchase of the U.S. Grant Hotel in downtown SD. STDC formed several LLCs under state law, American Property Investors LLC, that owns Sycuan Investors LLC that in turn owned U.S. Grant Hotel Ventures LLC who ultimately purchased the hotel. U.S. Grant Ventures entered contract with the plaintiff to manage the hotel;
- Purpose: U.S. Grant LLC’s sole purpose for creation was to purchase and operate the U.S. Grant Hotel

STATE INCORPORATED TRIBAL LLC – IS THE ENTITY AN “ARM OF THE TRIBE”?

- Structure, ownership, management and control by the tribe: U.S. Grant LLC is owned by Sycuan Investors LLC who in turn is owned by American Property Investors LLC who is owned by STDC. No tribal involvement with the LLC;
- Financial relationship between the tribe and the entity: the various corporate forms were created to purchase, own, manage and operate the hotel and sheltered tribal assets. The court looked at the primary purpose of immunity -- to protect the tribal coffers – and here there was no impact to tribal general funds. Liabilities would only be paid out of corporation assets;

STATE INCORPORATED TRIBAL LLC – IS THE ENTITY AN “ARM OF THE TRIBE”?

- Did the tribe intend for the entity to have tribal immunity: Court found nothing in the record to demonstrate that tribe intended any of the LLCs created to be covered by tribal immunity;
- Whether the purpose of tribal immunity is served by granting immunity to the entity: Court found none. The purpose was to operate a hotel and not to provide for the general welfare of the tribe or other economic development.

DEVELOPMENT OPPORTUNITIES

- Economic Development opportunities often come to the tribe in two ways:
 - Proactive development—tribe decides what business it wants to engage in and goes out and finds investors, partners, and brings the business to the tribe;
 - Reactive development—unsolicited proposals are presented to the tribe.

DEVELOPMENT OPPORTUNITIES

- Proactive is preferable:
 - What is the right business for the tribe –develop a General Plan;
 - What is the highest priority for establishing the business—building job skills, employment, generating revenue, or mixture;
 - What are the tribe’s resources —water, land, wind, solar, public accessibility, scenic beauty, habitat, recreational environment, close to market, strong workforce, etc.;
 - Time to conduct feasibility studies, business plan, consider financing options, research industry, evaluate similar businesses ;
 - Conduct due diligence on prospective partners, consultants, other players needed for the business;
 - Other....

DEVELOPMENT OPPORTUNITIES

- Reactive response to unsolicited business deal:
 - Time pressure is usually a factor—“must act now or the deal is lost”;
 - No time to do all of the planning and accessing necessary to properly evaluate the business;
 - Unsolicited proposals can take more to evaluate because it may be a new business area that was not contemplated by the tribe and tribe may need to get familiar with the business area;
 - Also, such proposals may be riskier because less may be known about the specifics being proposed, the developer, the financing, and other factors.

EVALUATING THE DEAL

- “Due Diligence”--- Know who you are dealing with at every stage of a development. What to ask and where to look:
 - Name of company or corporation representatives (Google)
 - Where incorporated, when, status, Articles of Incorporation (check Secretary of State website);
 - **References!** (contact other current and former clients);
 - If specialized business, check industry journals, publications, government agency that may have oversight of business (e.g. Department of Energy);
 - Feasibility studies that developer has done specific to proposed project for your tribe (why will the business be successful on your reservation);
 - Certificates of Insurance;
 - Have they been sued or sued a tribe, by their employees, by the government;
 - How did the developer learn about the tribe and why was tribe selected for the proposal.

EVALUATING THE DEAL

- “Due Diligence” ---
 - Who are the shareholders;
 - Annual reports;
 - Property owned by the developer, type, and where;
 - Tax returns, Audited Financial Reports for the last 5 years;
- What else would you want to ask???

EVALUATING THE DEAL

- Feasibility Study—will the business be successful? Critical for any proposed project the tribe is considering;
- Defined –“is an evaluation of proposed economic development projects conducted by 1) **qualified**, 2) **disinterested** 3) **third party**”;
- “Qualified”: Prepared by consultant that has the expertise pertaining to the project under consideration, has conducted similar studies before or has an academic or professional license or credential relevant to the project;
- “Disinterested”: The person has no financial or personal stake in the outcome of the study;
- “Third party”: Person is not a tribal member or an entity connected to the tribe.

EVALUATING THE DEAL

- What a feasibility study will assess (not complete list):
 - The market for the proposed project;
 - Likely consumers of the product or services;
 - Likely competitors;
 - Price consumers will likely pay;
 - How much of the market can the tribe capture;
 - Does tribe have sufficient capital available for the start up;
 - **What structure the tribe should choose to organize the business and how this might affect tribal sovereign immunity and tax liability**;
 - Will the return on investment be adequate to pay business or project financing costs.

EVALUATING THE DEAL

- Feasibility Study (continued):
- Helpful with:
 - Evaluating the success or failure of a project;
 - Making an informed decision;
 - Obtaining financing—demonstrates that the project is viable and risk is low to investors;
 - Membership's support of the project;

EVALUATING THE DEAL

- Cost of the study will vary depending on the project—but may cost several thousands of dollars;
- Check around for funding----
 - Department of Energy has (had) grant programs available for conducting feasibility of solar and other alternative energy projects on tribal lands.

RESEARCHING AND NETWORKING

- **Private:** Companies and lenders may be looking for investments.
 - *Native American Chamber of Commerce* is an example of a resource that might connect your tribe with opportunities and networking;
 - *Tribal Business Journal* -- publication;
 - Local persons with business experience may be willing to sit on your Board or act as a free consultant—they in turn may know someone.

RESEARCHING AND NETWORKING

- **Public:** Federal Guarantee Loan Programs are options—examples:
 - U.S. Department of the Interior Office of Indian Energy and Economic Development has an Indian Affairs Loan Guaranty and Insurance and Interest Subsidy Program that administers 2 loan programs. One offers a 90% loan guarantee of a lender's loan to a tribe "if the business activities will contribute to reservation economic development"
 - U.S. Department of Agriculture Business & Industry Loan Program—which charges a guarantee fee that is 2% of the original loan amount and is available to tribes for machinery and equipment, buildings and real estate, working capital, and certain refinancing. Program covers multi-million dollar loans;
 - Tax exempt bonds, Tax Credit Financing — see a specialist.

CONCLUSION

- Evaluate and consider possible economic development for your community, goals, purpose, tribal human resources and natural environment;
- Start now to put in place the economic infrastructure the tribe will need to have viable economic development;
- Get legal advice on how to structure your economic development entity to ensure sovereign immunity is preserved and tax exemption status protects tribal income and profits;
- Develop a process or protocol for evaluating development proposals—e.g. developer must provide XYZ before the tribe will entertain any proposal;
- Do your due diligence; and
- Learn from others and reach out for assistance from trusted sources.
-