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MEMORANDUM

February 23, 2016

TO: Kitcki Carroll

FROM: Michael Willis /s/ and Greg Smith /s/

RE: ***Tax Policy Developments***

This memorandum reports on the following tribal tax policy developments:

- ***Congressional appointments for the Treasury Tribal Advisory Committee still pending; Tribes call for Committee to begin its work***
- ***Agua Caliente v. Riverside County: Federal Court Applies Bracker Balancing Test in Concluding that Federal Law Preempts County Taxation of Non-Indian Lessees on Reservation Land***
- ***Assistant Secretary – Indian Affairs identifies revision of the Indian Trader Regulations as among the policy priorities for 2016***
- ***Tax parity continues to generate policy interest in Congress, the Administration and among Tribes***

Congressional appointments for the Treasury Tribal Advisory Committee still pending; Tribes call for Committee to begin its work

In December, the Department of the Treasury announced the appointment of three tribal representatives to serve on Treasury's Tribal Advisory Committee (TTAC). As established in the Tribal General Welfare Exclusion Act of 2014, the TTAC will advise the Secretary on matters related to the taxation of Indians, the training of Internal Revenue Service (IRS) field agents, and the development of training and technical assistance for tribal governments. The seven-member TTAC is made up of Treasury's three appointees and the four members appointed by Congress (the Chairs and Ranking Members of the Senate Finance Committee and the House Ways and Means Committee each appoint one TTAC member).

As we reported in our December 2015 tax policy memorandum, House Ways and Means Committee Ranking Member Levin (D-MI) has announced his appointment, but three of the seven TTAC members have not been named. These will be appointed by Senate Finance Committee Chairman Hatch (R-UT), Senate Finance Committee Ranking Member Wyden (D-OR) and House Ways and Means Chairman Brady (R-TX).

Earlier this month, Treasury Deputy Assistant Secretary Tom West (who has replaced Elaine Buckberg as Treasury's point of contact for tribal consultation) told tribal representatives that convening the TTAC was a top priority of the Department. His remarks to the United South and Eastern Tribes on February 9 asserted that the Department wants to convene the TTAC immediately, but believes it must wait until all seven members are appointed. Mr. West pointed out that the delay not only postpones the implementation of the education and training provisions of the Tribal General Welfare Exclusion Act, but it also limits Treasury's opportunity to begin engaging the TTAC on other tax policy issues of concern to Indian Country. Tribal representatives expressed they also view the TTAC as an urgent priority and that the Obama Administration should be sure to have the TTAC in place and in operation before leaving office.

As part of Impact Week, USET representatives visited with the offices of Chairmen Hatch and Brady and Ranking Member Wyden to urge that they finalize their appointments to the TTAC. The Senate Finance Committee leadership blamed their delays on the existing and constraining procedures the Committee has in place for Presidential appointments. Both Chairman Hatch and Senator Wyden's staff explained that they were streamlining that process and hope to present their nominees soon. Neither were willing to state a timeframe and both offices expressed willingness to consider suggestions regarding qualified tribal nominees. Chairman Brady's office indicated that his selection process was more agile than that of the Senate Finance leadership as it is not constrained by existing procedures. Nonetheless, Chairman Brady did not have a deadline for finalizing the appointment and also welcomed the submission of qualified nominees.

Three of the four named TTAC members (Ron Allen; Eugene Magnusun; and Lacy Horne met with tribal representatives during the National Congress of American Indians (NCAI) Executive Council Winter Session to discuss priorities for the TTAC. (Lynn Malerba was unable to attend). In addition to hearing concerns from tribal representatives about tax policy objectives, several attendees urged that the four named TTAC members begin meeting informally and engaging Indian Country to begin shaping a policy agenda. Comments included suggestions that a starting point would be to identify those issues where an administrative policy change or clarification by the Department would have widespread impact in Indian Country. TTAC members expressed an interest in beginning such an informal process.

***Agua Caliente v. Riverside County*: Federal Court Applies *Bracker* Balancing Test in Concluding that Federal Law Preempts County Taxation of Non-Indian Lessees on Reservation Land**

We have reported previously on several cases in which tribes have brought federal lawsuits to challenge state and local taxation on Indian lands. In *Agua Caliente v. Riverside County*, the tribe opposed the local government's imposition of a possessory interest tax ("PIT") on lessees of reservation trust lands. The PIT is general revenue tax

that is assessed against a person or entity who leases, rents, or uses real property that is otherwise owned by a governmental agency. On February 8, 2016, the U.S. District Court for the Central District of California concluded that Riverside County ("the County") could not impose a PIT on non-Indian lessees of reservation land because it was preempted by Supreme Court precedent under the *Bracker* balancing test. *Agua Caliente Band of Cahuilla Indians v. Riverside Cnty, et al.*, No. CV 14-0007 (C.D. Cal. Feb. 8, 2016).

The Supreme Court's decision in *White Mountain Apache Tribe v. Bracker* established a balancing test for assessing the validity of state taxation of non-Indian activities on reservation land. 448 U.S. 136 (1980). The test requires that courts conduct a "particularized inquiry" into the federal, state, and tribal interests at stake in order to determine whether the exercise of state taxing authority would violate federal law. *Id.* at 144-45. The inquiry includes, but is not limited to, a judicial analysis of relevant federal laws, potential impact on tribal economic development, and the existence of a nexus between the tax and the activity being taxed. Courts will reject the imposition of state taxes where strong federal and tribal interests are found to outweigh those of the state.

In *Agua Caliente*, the California District Court determined that application of the *Bracker* test prohibited the County from imposing a possessory interest tax on the Agua Caliente Band of Cahuilla Indians ("the Band") reservation land. In reaching its decision, the court undertook an extensive analysis of the *Bracker* balancing factors with attention given to preceding case law and the Bureau of Indian Affairs's (BIA) own interpretation of how state law affects the federal land leasing regulatory scheme. In particular, the court looked to the comprehensiveness of the federal regulatory scheme governing Indian leases, such as 25 U.S.C. § 415 (authorizing the leasing of Indian lands with Secretarial approval), 25 C.F.R. § 162.017 (prohibiting the imposition of taxes and other fees on any leasehold or possessory interest absent contrary federal law), and 25 U.S.C. § 465 (prohibiting the taxation of Indian lands held in trust by the federal government). The court concluded that federal regulation of leased Indian lands "is both detailed and pervasive, and there is no indication that Congress has delegated any authority over the leasing of Indian lands to the States." *Agua Caliente*, No. CV 14-0007 at *20.

The court moreover found that the tribal interests of the Agua Band Caliente were persuasively strong under the circumstances of the case. The court considered the high number of leases that the Band currently holds and the fact that it had withheld from imposing its own taxes on those leases in order to avoid double taxation and concluded that these factors "constitute[] a strong tribal interest which would be frustrated by the imposition of the County's PIT." *Agua Caliente*, No. CV 14-0007 at *21. In contrast, the court noted that the County lacked persuasive factors in its favor and held "[t]he County's general interest in raising revenue…is not sufficient to overcome the strong tribal and federal interests at stake." *Id.* at *22.

The California District Court's decision marks the continued development of the post-*Bracker* line of cases that reject the proposition that an express congressional statement is required in order find federal preemption of state law. The court's decision and its application of the *Bracker* balancing test in analyzing the recently revised federal land leasing regulations offers important guidance that may help tribes further their economic development through the generation of leasing revenues in Indian Country that are free from double taxation by state or local governments. As in the Eleventh Circuit case, *Seminole Tribe of Florida v. Stanburg*, the BIA's land leasing regulations were entitled to deference and served to demonstrate strong federal and tribal interests with respect to the leasing of tribal trust lands. Because of *Bracker's* requirement of a "particularized inquiry," however, the court could not rely upon the preemptive force of the regulations themselves. Instead, the court analyzed the specific federal, tribal and state interests associated with the tax under the balancing test that has been in place since 1980 and found the BIA's land leasing regulations and its taxation provisions to express strong federal and tribal interests that outweighed those of the local government.

Assistant Secretary – Indian Affairs identifies revision of the Indian Trader Regulations as among the policy priorities for 2016

On February 22, Assistant Secretary-Indian Affairs Larry Roberts presented the Administration's top priorities for Indian Country to tribal representatives attending NCAI's Executive Council Winter Session in Washington, DC. The Assistant Secretary stated that a revision to the outdated Indian Trader regulations was an area of interest. The revision to the regulations would be undertaken in part to set forth the federal and tribal interests in regulating commerce on Indian lands and to clarify the tax jurisdiction of tribes in those lands to the exclusion of state and local taxation. The effort would be seen as providing an opportunity to include taxation terms similar to those adopted in the BIA Land Leasing Regulations, 25 C.F.R. Part 162 (discussed above), and the Right-of-Way Regulations, 25 C.F.R. Part 169.

Revision of the Indian Trader regulations has been an approach recommended by a number of tribal advocates and adopted as a policy priority by NCAI. NCAI has submitted proposed regulations to the Department of Interior for consideration (please see our December 2015 report for details). NCAI representatives suggested that Interior has set a goal of promulgating draft rules late in the spring of 2016. We will provide further updates and details on developments and perspectives on this process in our next report.

Tax parity continues to generate policy interest in Congress, the Administration, and among Tribes

In a number of policy areas the federal tax code contains restrictions on tribal governments which are not applicable to state governments. These restrictions on tribal governments have impeded tribal economic growth and development. In the last

Congress, several bills, including H.R. 3030 (introduced by Rep. Kind (D-WI), set forth tax code changes that would treat tribal governments in a manner consistent with their state government counterparts in such areas as: tax-exempt bonds, governmental retirement plans, and public charities. Other legislation would have empowered tribal governments, just like their state counterparts, to make the determination that a child has special needs for the purposes of an adoption tax credit while another bill would have addressed the taxability of the Indian Health Service loan repayment programs.

Rep. Kind has indicated interest in reintroducing H.R. 3030 and tribal advocates have been meeting with House Ways and Means Committee Members to identify Republican co-sponsors. Additionally, NCAI and other tribal advocates have encouraged Rep. Kind to broaden H.R. 3030 to comprehensively address tax parity issues by including provisions, such as the adoption tax credit and Indian Health Service (IHS) loan repayment terms, into his bill.

Administration's Proposals. In the FY 2017 budget, the Administration has supported amendment of several provisions to enhance parity. Among those are:

- Repeal the existing "essential governmental function" standard for tribal governmental tax-exempt bond financing.[1] This would adopt the State or local government standard for tax-exempt governmental bonds without a bond volume cap on such governmental bonds.
- Allow tribal governments to issue tax-exempt private activity bonds for the same types of projects and activities as are allowed for State and local governments under a national bond volume cap.
- Treat tribal governments as state governments with regard to information sharing for tax compliance and administration purposes.
- Improve disclosure to facilitate child support enforcement.
- Empower tribal governments, just like their state counterparts, to make the determination that a child has special needs for the purposes of an adoption tax credit.
- Make tax-exempt the IHS Health Professions Scholarship Program and Loan Repayment Program, thus not requiring recipients to count the benefits in their gross income. This would be similar to the tax treatment afforded recipients of the National Health Service Corps and the Armed Forces Health Professions

[1] Treasury, in its 2011 report to Congress on Tribal Economic Development Bonds, has previously called for elimination of the "essential governmental functions" limitation with respect to tax exempt bonds and made additional recommendations. The FY 2017 budget request incorporates and expands upon the recommendations from that report.

scholarships. Also, to exempt recipients from the Federal Employment Tax just as is afforded the National Health Service Corps.

Administration's Actions. A recent report regarding the Department of Labor issuing penalties to tribes for non-compliance with the Pension Protection Act (PPA) regarding tribal governmental retirement plans is increasing the urgency for the legislative fix envisioned in Rep. Kind's H.R. 3030. Rather than engage in consultation to establish regulations regarding the PPA's "essential governmental function" and commercial function distinction, the DOL is engaging in case-by-case enforcement action, which DOL deems not appropriate for consultation. Tribal representatives at NCAI urged that DOL be engaged to change this position. The reintroduction of H.R. 3030 and its passage was identified as the critical legislation to resolve this controversy.

In the tax-writing committees, tax policy staff have indicated that while comprehensive tax reform is not on the agenda for 2016, there may be an appetite for specific legislation on discrete matters. Chairman Hatch's staff confirmed that tribal governmental tax parity with state governments is among the tribal tax priorities that Committee leadership recognizes and has interest in addressing. When and whether the political moment will take shape this year or in the next remains to be seen. The effort by Rep. Kind and potential co-sponsors would move the ball in the right direction.

Conclusion

We will continue to monitor tax developments on your behalf. Please contact us if you have any comments or questions.