



Native American Finance Officers Association

Growing tribal economies. Strengthening tribal finance.

1101 30th Street, NW, Suite 500 • Washington, DC

December 19, 2018

Mr. Scott Dindwiddle
Office of the Associate Chief Counsel
Income Tax & Accounting
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D.C. 20224

RE: IRS REG-115420-18
Recommendations for the Proposed Opportunity Zones Regulations

Dear Mr. Scott Dinwiddle:

In representing the economic interests of over one hundred tribal governments, NAFOA has a clear mission to build and grow tribal government economies by advocating for effective economic policy solutions. In furtherance of our mission, we welcome the opportunity to comment on the proposed Opportunity Zones regulations. Our recommendations will ensure that this new initiative is successful for economically distressed communities in Indian Country, where 366 designated Opportunity Zones areas overlap with tribal lands. We also believe that our recommendations are necessary for the successful implementation of the program by the Department of the Treasury (Treasury) and the Internal Revenue Service (IRS).

Since the passage of the Tax Cuts and Jobs Act of 2017 (Pub. L. 115-97), NAFOA has been active in disseminating information to tribal governments and facilitating discussions about Opportunity Zones. NAFOA has hosted webinars and in-person discussions with tribal government representatives, as well as with the investment community, the community development finance field, and other related organizations. Through these outreach efforts, NAFOA has received significant feedback critical to developing clear recommendations on how to modify the proposed Opportunity Zones regulations to ensure that tribal governments can

successfully benefit from the program. Tribal governments occupy some of the most distressed areas in the United States, including eight of the ten most distressed areas in our nation. **As the regulations currently are written, tribal governments are at risk of being excluded from what promises to be significant investment in distressed communities.**

Background

Tribal governments are in some of the most economically disadvantaged areas in the country, with high levels of generational poverty and unemployment. Despite past federal programs and policies aimed at improving the quality of life in America, such as Enterprise Zones, Promise Zones, and the New Markets Tax Credits program, none have met their goal of impacting tribal communities in significant ways. These federal programs have fallen short in Indian Country because they lack adequate access to capital and incentives to do business in Indian Country, and most troubling, tax credits and other programs fail to include requirements that meet the needs of tribal governments. This failure to include tribal governments is often an oversight, but a very costly one to Indian Country. Unless tribal governments are specifically listed and accounted for in laws and regulations, they are often considered excluded in practice.

Economic development, specifically through tribal enterprises, is especially important in Indian Country since 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 enterprises to provide government services such as public safety, education, housing, and cultural programs. It also makes programs that invest capital – like Opportunity Zones - even more valuable for Indian Country.

Finally, tribal governments also lack access to effective and affordable capital. Financing for needed healthcare centers, tourism projects, and infrastructure is difficult to come by. Even when financing is obtained, it is often inadequate, meaning that projects are often delayed, not built to their full capacity, funded in more costly ways, or, in some cases, never built at all.

Recommendations

1. Lease Valuation Clarification - Leases of tangible property must be considered Qualified Opportunity Zone Business Property and count towards the 70% tangible property requirement in the business property definition (1400Z-2(d)(3)(A)(i)).
2. Eligible Entities Inclusion - Tribal governments must be included in the eligible entities that can form a corporation or partnership for Qualified Opportunity Funds.

3. Tribal Consultation - Treasury and IRS must conduct tribal consultation as soon as possible to ensure that they satisfy Treasury's Consultation Policy and gather input directly from tribal governments.

Lease Valuation Clarification - Rules for Qualified Opportunity Zone Property in Qualified Opportunity Funds

The proposed regulations on property requirements may have the unintended consequence of excluding investments on tribal lands. Tribal governments occupy federal trust lands and these lands are, more often than not, leased for economic development purposes. Lease agreements are used to generate revenue for the tribe through ranching, energy development, tourism, external business partnerships and many other development projects. Therefore, it is essential that the Opportunity Zones regulations modify the Qualified Opportunity Zone business proposed property rules to include leased property.

For background, the Secretary of the Department of the Interior manages the use and benefit of approximately 60 million acres of Indian land. This "right" to use reservation land generally resulted from treaties, executive orders, and similar arrangements between a tribe and the U.S. government. These trust arrangements provide a tribe with the beneficial use of the lands, but they do not convey ownership. As a result, most reservation land does not have a value and is not reported on a tribe's financial statements. The proposed regulations currently state that an Opportunity Fund must have 90% of its assets in Opportunity Zone property and 70% of it must be tangible or real property. Trust lands may not be sold or encumbered, therefore, valuing the lease of trust lands for the purposes of Qualified Opportunity Zone property is not an appropriate measure of tangible assets for tribal governments. Leases of land and buildings as tangible property is essential. Without immediate correction, the tax benefits may be too small for an investor to justify the startup capital to invest in Indian Country.

The foundational principle of leases is that they are financings – the right to use the underlying asset for more than a 12-month period. NAFOA recommends that the financing agreement secured by a leasehold interest count towards the 70% asset test as long as the lease met the definition as defined by GASB 87 and FASB ASC 842.

To illustrate why this is problematic for tribal governments, assume that on January 20, 2018, Tribal Invest Fund (a Qualified Opportunity Fund) will lease land and a building on a reservation with the intent of turning it into a grocery store. The value of the land and building lease is \$500k (\$380k attributed to land and \$120k attributed to the building). Again, keep in mind that the legal title of the reservation land is held by the federal government. The Tribal Invest Fund would

record a one-time “Right of Use Asset” on their financial statements for the value of the lease at \$800k. If the lease of tangible property in this example did not qualify, the investor would need to inject an additional \$1.17m into the Opportunity Fund to meet the 70% tangible property requirement. This hurdle will deter potential investors unless there is clarity that leases of real property qualify. As illustrated, the exclusion will devastate tribal government participation in Opportunity Zones and is inconsistent with the policy objectives of the program – to encourage economic growth and investment in distressed communities.

An additional point that further demonstrates the importance of leases counting towards the tangible property requirement lies in one of the most substantial expenses to a business – operating costs. For businesses locating on a reservation, many investments create intangible assets that are necessary such as salaries, health insurance, liability insurance, software, marketing, website fees for e-commerce, and other uses that will not be considered qualified opportunity zone business property. Likely the extent to tangible property without lease considerations would only include computer equipment and furniture. Again, the proposed rules unfairly prioritizes tangible property, and without clarity on leases, it is unrealistic that any business located on a reservation would meet the 70% asset test.

Leases of tangible property must be considered Qualified Opportunity Zone Business Property and count towards the 70% property requirement in the business property definition (1400Z-2(d)(3)(A)(i)).

Eligible Entities Inclusion - Rules for a Qualified Opportunity Fund

Another major concern is the exclusion of tribal governments as eligible entities for creating Qualified Opportunity Fund corporations or partnerships. Currently, the proposed regulations state that a Qualified Opportunity Fund must be a corporation or partnership created or organized within the 50 states, the District of Columbia, or a U.S. possession. The U.S. possession is further defined as any jurisdiction outside of the 50 states and the District of Columbia and may include U.S. territories such as Guam, Puerto Rico, the U.S. Virgin Islands, Northern Mariana Islands, and American Samoa.

Tribal governments are distinct political entities that have the power to self-govern and exercise sovereignty over their citizens and territory. As sovereign nations, tribal governments have powers and capabilities not available to other individuals in the United States. This sovereignty is recognized in the Constitution, treaties, and judicial decisions. As such, tribal governments can form a governmental entity to perform business functions to generate revenue for funding government functions and programs. As mentioned above, revenues from economic enterprises

act as a replacement for tax revenues, since tribes do not have a tax base. Many tribes conduct business activities through tribally-chartered corporations or federally-chartered corporations formed under Section 17 of the Indian Reorganization Act. Due to their unique status, if a tribal government cannot create a Qualified Opportunity Fund entity within its jurisdiction, tribes will be unable to participate in creating Opportunity Funds. This lack of self-determination means tribal governments may miss out on lease and potential tax revenue and may have more difficulty aggregating projects to meet the needs of their communities.

The ability of tribal governments to charter corporations and partnerships as Qualified Opportunity Funds, like their state and territorial government counterparts, will define the success of Opportunity Zones in Indian Country. The selection of structure will significantly influence the way the Opportunity Zone Fund at a tribal government operates, impacting everything from legal liabilities, to tax treatment, to governance and financial reporting – all critical factors in attracting potential investors. Tribal governments must be included in the eligible entities that can form a corporation or partnership for Qualified Opportunity Funds.

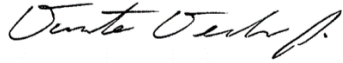
Meaningful Tribal Consultation

Opportunity Zones has the potential to direct much-needed capital to Indian Country, which includes some of the most distressed low-income communities in the United States. Given the large number of tribal governments located within designated Opportunity Zones, 366 in total and 190 in middle America, we recommend that Treasury and the IRS host a consultation session with tribal leaders prior to releasing the final regulations. Failing to consult directly with tribal governments on this matter before deciding on the final regulations is inconsistent with Treasury’s adopted Tribal Consultation Policy 80 Fed. Reg. 57434-57436 (Sept. 23, 2015), which states that “Treasury will consult with Tribal Officials before implementing Policies that have Tribal Implications.” *Id.* at 57435 (2015).

Consultation has led to favorable outcomes for both the federal government and for tribal governments in recent years and we believe that would be true in the case of Opportunity Zones. NAFOA appreciates the continued commitment, dedication, and outreach of Treasury and the IRS. This partnership has proven to be effective in making sure tribal governments are included in federal initiatives and for ensuring programs are effective in Indian Country. Treasury and the IRS should conduct tribal consultation as soon as possible to ensure that they satisfy Treasury’s Consultation Policy and gather input directly from tribal governments that is sure to make this program successful for tribal governments.

We greatly appreciate the opportunity to submit comments and recommendations to ensure the program's success for all communities and clarify guidance for investors in economically distressed communities.

Sincerely,

A handwritten signature in black ink, appearing to read "Dante Desiderio".

Dante Desiderio
Executive Director, NAFOA

Attachments: List of designated opportunity zones located within tribal lands.