STRUCTURING TRIBAL BUSINESS ENTERPRISES AND JOINT VENTURES

April 22, 2009

Prepared by

Kathleen M. Nilles, Esq.
Holland & Knight, LLP

Karen J. Atkinson, Esq.
Native American Contractors Association

For the National Renewable Energy Laboratory (NREL) under a subcontract with Alliance for Sustainable Energy LLC

OVERVIEW - STRUCTURING TRIBAL BUSINESS*

- Key Factors in Choosing a Structure
- Available Types of Corporate and Governmental Structures
- Pros and Cons of Each Structure
- Special Considerations Applicable to Joint Ventures

* This PowerPoint Presentation is based on concepts presented and detailed in the Tribal Business Structure Handbook, co-authored by Karen Atkinson and Kathleen Nilles (© 2008, 2009). The 2009 edition of the Handbook is available for purchase at www.nafoa.org/publications.

.

CHOICE OF BUSINESS STRUCTURES

- Why is it important?
- Determines how a tribe will interact with non-Indian businesses or partners
- A non-Indian partner needs to know the type of tribal organization

KEY FACTORS TO CONSIDER

- Organizational Considerations
  - Ease of Formation
  - Governance and Management
- State and Federal Tax Treatment
  - Income Tax Immunity of the Entity
  - Availability of Tax Incentives for Project
  - State Income and Sales Taxes
  - Fed/State Excise Taxes

KEY FACTORS TO CONSIDER (continued)

- Facilitating Financing/Access to Capital
- Immunity and Limitation of Liability
  - Protection of Tribal Assets
  - Limitation of Liability For Non-Tribal Owners
  - Resolution of Disputes (choice of law, forum, etc.)

THREE TYPES OF GOVERNMENTAL ENTITIES

- Tribal Government
- Unincorporated Agencies, Divisions, Enterprises and Instrumentalities of the Tribal Government
- Political Subdivision of Tribal Government

THREE FORMS OF BUSINESS ENTITIES

- Corporation
- Partnership
- Limited Liability Company (LLC)

TRIBAL GOVERNMENT AS A BUSINESS ENTITY

- Tribes have inherent rights of self-government, including the power to engage in business and commercial activities
- Easy to organize, but no separation of business from politics
- IRS has consistently ruled that the Tribe is not a taxable entity (Rev. Rul. 94-16 at www.irs.gov/pub/irs-tege/rr94_16.pdf)
  - Income derived from any business operated directly by a Tribe (on or off Tribe's reservation) will be tax free
  - In general, no tax incentives available to non taxpayers
  - Excise tax exemptions generally limited to essential governmental funds

TRIBAL GOVERNMENT AS A BUSINESS ENTITY

- Tribal Governments possess sovereign immunity from suit (Santa Clara Pueblo v. Martinez, 436 U.S. 49 (1978))
- Federally recognized Indian tribal governments (ITGs) also have <u>some</u> access to tax-exempt or tax-favored financing
  - Tax-exempt bond financing authority (use limited to essential governmental functions) (26 U.S.C. § 7871)
  - Clean renewable energy bonds ("CREBs) (use not limited to essential governmental functions, but Tribe must <u>apply</u> to Treasury for an allocation 26 U.S.C. § 54(a)

UNINCORPORATED AGENCIES, DIVISIONS AND INSTRUMENTALITIES

- Tribe may operate a business enterprise tax-free through an agency, unincorporated division, or an instrumentality – i.e., as an arm of Tribal government that is not considered a distinct legal entity
- Generally, these governmental units are formed under tribal law for governmental purposes, including economic development (e.g., a tribal utility)
- Share the same legal characteristics as the tribal government because they are generally not separate legal entities

UNINCORPORATED AGENCIES, DIVISIONS AND INSTRUMENTALITIES (Management)

- These governmental units are usually controlled by the tribal government and its tribal council
- May have a board of directors, which is usually comprised of tribal council members and others
- Manager in charge of day-to-day activities

UNINCORPORATED AGENCIES, DIVISIONS AND INSTRUMENTALITIES (Immunity)

- Just as Indian tribes posses sovereign immunity from lawsuits, a governmental unit that serves as the tribe's economic arm possess the same immunity
- Consequently, these units cannot be sued absent a clear waiver of immunity (Kiowa Tribe of Oklahoma v. Manufacturing Technologies, Inc., 523 U.S. 751 (1998))
- Immunity can create uncertainty and risks for nontribal partners and lenders

UNINCORPORATED AGENCIES, DIVISIONS AND INSTRUMENTALITIES (Tax Treatment)

- IRS has consistently ruled that the Tribe is not a taxable entity (Rev. Rul. 94-16)
- Tribal governmental units have been treated the same as tribes because they are not a separate legal entities
- There is no specific exemption for business enterprises wholly-owned by Tribes
- Instead, tribal business enterprises are exempt so long as they are operating arms of the Tribe

UNINCORPORATED AGENCIES, DIVISIONS AND INSTRUMENTALITIES (Tax Treatment)

- When determining tax treatment of an instrumentality, the IRS looks at the following:
  - Governmental purpose or function
  - Performance of function on behalf of the tribal government
  - Whether the tribal government has the power and interest of an owner

UNINCORPORATED AGENCIES, DIVISIONS AND INSTRUMENTALITIES (Tax Treatment)

  – Control and supervision by tribal government

  – Statutory authority for the instrumentality’s creation and operation

  – Degree of financial autonomy and source of operating expenses

- <u>See</u> Rev. Rul. 57-128, 1957-1C.B.311 and PLR 200621010 (Feb. 1, 2006) (www.irs.gov/pub.irs-wd/0621010.pdf)

PROS AND CONS

- Advantages:
  - Relative certainty of tax treatment
  - Same federal privileges and immunities as tribe
  - Access to federally subsidized financing (including tax-exempt and/or tax-credit bonds)
- Disadvantages:
  - Governance issues (e.g., some mixing of business and politics)
  - Requirements of partners and lenders

POLITICAL SUBDIVISIONS

- A political subdivision is a unit of the tribal government that:
  - Is separate from the government
  - Has been delegated a sufficient amount of one or more recognized sovereign powers of the tribe
  - Created under tribal law to fulfill a substantial governmental function of the government (e.g., a utility that performs regulatory functions)
  - Has same tax-free status as the Tribe
- See Rev. Proc. 84-37, 1984-1 C.B. 513 (ww.irs.gov/pub/irs-tege/rp1984_37.pdf)

POLITICAL SUBDIVISIONS (continued)

- Tribal political subdivision must exercise one or more sovereign powers:
  - Power to tax
  - Power of eminent domain
  - Power to regulate
- As set forth in Rev. Proc. 84-37, there are two steps to confirming a political subdivision's status
  - Secure a letter from the DOI verifying that the Tribe has delegated a substantial government power
  - Once the letter has been issued, file a ruling request with the IRS

POLITICAL SUBDIVISIONS (continued)

- IRS treats political subdivisions the same as the tribe—so long as they qualify as such by having been delegated substantial government powers
- Political subdivision shares in other tax benefits under IRC §7871
  - Tax-exempt bond authority
  - Excise tax exemptions
- Political subdivisions are eligible for other tax-favored financing

PROS AND CONS

- Advantages of a political subdivision
  - Relative certainty of federal tax treatment
  - Possible retention of state tax immunity
  - Can use political subdivision as both a regulatory body and as a business holding company
  - Availability of federally subsidized financing, such as Clean Renewable Energy Bonds (“CREBs”)

PROS AND CONS (continued)

- Disadvantages of a political subdivision
  - Time and expense of formation, including dual federal agency approval
  - Not as flexible a regular business entity
  - Business partners may not be comfortable dealing with a governmental entity

TRIBAL BUSINESS CORPORATIONS

- Federal Law Corporations
- State Law Corporations
- Tribal Law Corporations

FEDERAL LAW CORPORATIONS

- Section 17 of Indian Reorganization Act (IRA)
  - Formerly available only to tribes that had elected to organize their government under the IRA
  - Since 1990, available to non-IRA tribes and Alaska Native Communities (See 25 U.S.C. § 477)
- Section 3 of the Oklahoma Indian Welfare Act
- Can be utilized as an operating company or a holding company for one or more tribal subsidiaries (including an energy business) (See 25 U.S.C. § 501-509)

SECTION 17 CORPORATION

- Indian tribes must take the following five steps to organize and secure BIA approval of a federally-chartered Section 17 corporation (25 U.S.C § 477; 25 C.F.R. Part 82):
  - Tribal Resolution or Petition
  - Draft Charter
  - Approval by the Tribe
  - Filing of Petition/Resolution
  - Ratification of Corporate Charter

SECTION 17 CORPORATION (Management)

- Federally-chartered corporations are separate legal entities that share the tribe's tax status and immunity
- Must be wholly-owned by the tribal government (<u>no</u> private ownership)
- Managed and controlled by a corporate board of directors appointed by the tribal government
- CEO or manager in charge of day-to-day operations

SECTION 17 CORPORATION (Immunity)

- Corporation vested with the same privileges and immunities as the tribe, including immunity from suit
- Section 17 charter must contain a “sue and be sued clause” permitting it to be sued in its corporate name
- Sovereign immunity waiver should be limited to <u>corporate</u> sovereign immunity and/or specific <u>transactions</u> entered into by the Section 17 corporation

PROS AND CONS

- Advantages
  - Same federal tax treatment as Tribe (Rev. Rul. 94-16)
  - Segregates assets and liabilities of business from tribal assets
  - If properly organized, a Section 17 corporation is immune from suit, but may waive immunity (Kiowa Tribe of Oklahoma v. Manufacturing Technologies, Inc., 523 U.S. 751 (1998))
  - 25 year leasing authority
    - Section 81 approval not necessary for leases or mortgages of tribal land (25 C.F.R. § 84.004(b))

PROS AND CONS (continued)

- Disadvantages
  - Charter approval process may be lengthy
  - Once a charter is issued by the Department of Interior (DOI) it can only be revoked by Congress
  - Business partners and lenders may be unfamiliar with federal chartering (e.g., no accessible DOI database of approved charters)
  - Availability of financing (e.g., not a qualified issuer of CREBs, but may be viewed as an instrumentality)

STATE LAW CORPORATIONS

- Corporation formed under state business or nonprofit corporation laws
- May be wholly owned and controlled by tribe, or it may be partially owned by the tribe and partially owned by other entities and individuals
- State law corporation is subject to state corporate law
- Most likely unable to assert tribe’s sovereign immunity

STATE LAW CORPORATIONS (continued)

- Taxable if incorporated under state law
  - Rev. Rul. 94-16 -- state-law corporation with Tribe as sole shareholder not tax-free
  - PLR 9826005 - wholly-owned nonprofit health corporation <u>not</u> an integral part of Tribe where formed under state law

    (www.irs.gov/pub/irs-tege/plr_9826005.pdf)
- States can form state-law corporations that qualify as “integral parts,” but tribes cannot (under IRS guidance issued to date)

PROS AND CONS

- Advantages of State-law corporations
  - Easily and quickly organized
  - Familiar to lenders and potential business partners
  - May facilitate a merger
- Disadvantages
  - Subject to federal income tax
  - Not a qualified issuer of tax-exempt financing
  - Not likely immune from suit

TRIBAL LAW CORPORATIONS

- Tribal law corporations are formed under a tribe's corporate code
- Tribal law corporations have been used with increasing frequency
- Relatively easy to establish, as compared to federally chartered corporations
- Tribal law corporations, unlike state law entities, are more likely to be free from state regulation (so long as business operations are confined to reservation)

TRIBAL LAW CORPORATIONS (Management)

- While the tribe is often the only shareholder, the corporation is managed by its own board of directors
- Tribal law corporations are managed and overseen by a corporate board of directors that are elected by the corporation's shareholders
- Directors approve budgets, approve the hiring and firing of setting compensation for senior officials, and establishing a business strategy
- A CEO or executive director manages the day-to-day operations of the corporation

TRIBAL LAW CORPORATIONS (Tax Treatment)

- Since 1994, income tax status has been uncertain
  - Rev. Rul. 94-16 did not address
  - In 1996, classification of entity regulations did not address, but preamble noted that Treasury and IRS were studying issue (26 C.F.R. § 7701-2)
- In 2001, Treasury/IRS agreed to resolve the uncertainty.
  - Progress on the pending IRS guidance has been slow

TRIBAL LAW CORPORATIONS (Tax Treatment)

- IRS could take one of three possible approaches
  - Treat like federally-chartered corporation (per se approach)
  - Apply Integral Part test (facts and circumstances)
  - Treat like state chartered corporation (negative per se)
- Integral Part Factors (IRS Version)
  - Whether Tribe has substantial governance control over entity
  - Whether Tribe has made a significant financial commitment to entity

TRIBAL LAW CORPORATIONS (Tax Treatment)

- “Integral Part” test is also used to determine tax treatment of state and local government-owned business entities
- IRS has enlarged its pending guidance project to cover all government-owned corporations and changed the form of guidance from a ruling to proposed regulations
- However, while the new proposed regulations are being formulated, the IRS has stopped issuing “integral part” rulings to both tribal government-owned and state government owned corporations
- Thus, tax uncertainty persists

PROS AND CONS

- Advantages of tribal law corporations
  - Ease of formation
  - Tribal sovereignty and less likelihood of state regulation
  - Flexibility
  - Possible tax immunity

PROS AND CONS (continued)

- Disadvantages
  - Uncertainty of federal tax treatment
  - Business partners may not be comfortable
  - Uncertainty of sovereign immunity
  - Availability of financing

ANOTHER OPTION: LIMITED LIABILITY COMPANY (LLC)

- An increasingly popular choice of business entity
- Commonly used for energy projects
- LLCs provide their owners with limited liability (like a corporation) but are not subject to double taxation
- Generally, formed under state law, but may also be formed under tribal law if tribe has an LLC code
- If subject to state law, sovereign immunity may not available

ANOTHER OPTION: LIMITED LIABILITY COMPANY (LLC) (continued)

- Formation requirements are similar to corporations
  - Can be quickly and easily organized under the laws of most states (or a tribal LLC code)
  - Must select a name and file a document similar to a corporation’s Articles of Incorporation
- May be wholly owned and controlled by tribe, or it may be partially owned by the tribe and partially owned by other entities and individuals

LIMITED LIABILITY COMPANY (Tax Treatment)

- Federal tax treatment of LLCs is provided for under the Treasury Regulations, which are sometimes referred to as the “check-the-box” regulations (26 C.F.R. §§ 301.7701-2 and 301.7701-3)
- If owned by two or more members, taxed like a partnership
- If wholly-owned, “disregarded” as a separate legal entity
- May elect to be taxed as a corporation

SINGLE-MEMBER ("SM") LLCs

- State and local government SM LLCs are treated like corporations under IRS regulations; IRS has also extended the per se corporation rule to foreign government SM LLCs
- So far, IRS has not extended this rule to tribal SM LLCs
- Most advisors believe that tribal government SM LLCs should continue to be treated as disregarded entities under current law, but IRS could change the rules (prospectively)

LIMITED LIABILITY COMPANY (Immunity)

- Under state LLC codes, an LLC's liability is limited to the assets of the company, thereby protecting the owners or members
- At least two courts have suggested that a tribe's sovereign immunity does not extend to its wholly-owned state-law LLCs

See Tribal Business Structure Handbook Appendix A (Sovereign Immunity Factors in Recent Judicial Decisions), available at www.nafoa.org/publications.

PROS AND CONS OF LLCs

- Advantages
  - Easily and quickly organized
  - Familiar to lenders and potential business partners
  - Can be used to acquire or merge with an existing state-law entity
  - Private financing available

PROS AND CONS of LLCs (continued)

- Disadvantages
  - Probably not immune from suit
  - Future taxation is somewhat uncertain
  - Federally subsidized financing, such as tax-exempt bonds and tax-credit bonds, may not be available

S CORPORATIONS

- S corporations are also used to achieve a single level of tax
- Not a viable option for tribal ownership
  - Tax Code restricts S Corp ownership to individuals, estates, trusts, pension plans and charitable organizations.
  - Rev. Rul. 2004-50 clarifies that a tribal government is not a qualified S corp. shareholder (www.irs.gov/pub/irs-drop/rr-04-50.pdf)

JOINT VENTURES

- Choice of entity
  - – Corporation (generally not tax-efficient)
  - – Partnership (flow-through tax treatment)
  - – LLC (same as partnership)
- Formation (choice of law)
  - – State
  - – Tribal

JOINT VENTURES (continued)

- As previously discussed, an LLC can be easily and quickly organized
- To organize, must select a name and file a document that is similar to a corporation's Articles of Incorporation

JOINT VENTURES (continued)

- May also form JV as a general or limited partnership
- General partnerships are easily organized (do not even have to file with the state), but each partner assumes liability for the activities of the organization

JOINT VENTURES (continued)

- Limited partnerships have one or more limited partners and at least one general partner
  - Limited partners are protected against personal liability for the partnership's activities
  - Limited partners cannot participate in the management and control of the business
  - General partner assumes liability for the partnership's business activities
  - General partner manages and controls the business

JOINT VENTURES (continued)

- Considerations common to LLCs and LPs
  – Whether to own the JV interest directly or through an intermediary business entity
  – Because of the tribe’s sovereign immunity and other uncertainties, business partners may prefer that the tribe hold its interest through a separate business entity
  – Sovereign immunity does not extend to the JV itself
  – But JV can be structured to minimize liability of owners

JOINT VENTURES (continued)

- Considerations common to LLCs and LPs (continued)
  - A JV would not be able to issue tax-exempt bonds or CREBs or use the proceeds of such an offering
  - Types of financing available
    - Private placements
    - Commercial bank financing
    - Government-guaranteed loans (depending on JV's line of business)

JOINT VENTURES (Tax Treatment)

- Under IRS regulations, the default classification for an LLC with two or more members is to be treated as a partnership
- If a Tribe is a member of a partnership (or an LLC treated as partnership), it will not be taxed on its share of JV's gross income
- Tribe and its JV partner can structure how profits and losses, deductions and tax credits are allocated – but only <u>within</u> <u>limits</u>
  - "Substantial economic effect" constraint
  - Tax-exempt entity leasing rules

PROS AND CONS

- Advantages of conducting economic development and business activities through a jointly-owned LLC or LP
  - Ease of formation
  - Flexibility (relative ability to design own governance structure
  - Flow-through taxation, which results in
    - Tribe’s share of the JV’s income being tax-free
    - Other partner’s share of tax benefits (e.g., deductions, credits) being available to it

PROS AND CONS (continued)

- Disadvantages
  - Likely loss of sovereign immunity
  - Inability to qualify for certain types financing
  - Difficulties in unwinding the JV if one party wants to terminate
  - Complicated tax rules apply if parties make disproportionate allocations of tax credits or other tax benefits

RENEWABLE ENERGY TAX INCENTIVES

- There a number of federal tax incentives available for the installation and production of renewable energy technologies, particularly on tribal lands
- Incentives can sometimes make the difference between a non-viable and a viable project
- Most incentives are designed as tax credits; however, it may still be possible for non-taxable entities, such as Indian tribes or enterprises, to capture the value of a credit by establishing a facility owned by a taxable entity or through other project structures

KEY INCENTIVES

- Accelerated Depreciation for Reservation Business Property and Infrastructure
- Section 45 Renewable Energy Tax Credit (Production Tax Credit)
  - Alternative #1: Investment Tax Credit
  - Alternative # 2: Treasury Grant
- Clean Renewable Energy Bonds
- New Markets Tax Credit

ACCELERATED DEPRECIATION FOR INDIAN RESERVATIONS FACILITIES OR INFRASTRUCTURE (Section 168(j))

- IRC 168(j) allows accelerated depreciation deductions for certain investments in business facilities and equipment and infrastructure property used to support an on-reservation trade or business
- Nature of the incentive
  - Allows the owner of qualifying property to take a faster write-off of the cost of such property
  - Reduces the owner’s taxes in the early years
- Implications for tribes
  - May only be used by a taxable entity
  - Can be a significant benefit for taxable entities (especially if combined with applicable tax credits, such as Section 45 credit)
  - Would not be applicable to an Indian tribe unless it is working with a taxable entity

SECTION 45 PRODUCTION TAX CREDIT ("PTC")

- Available to private entities subject to taxation for the production and sale of electricity from various renewable technologies
- Applies to the production of:
  - Wind
  - Open-loop biomass
  - Geothermal energy
  - Solar energy
  - Small irrigation
  - Municipal Solid Waste
  - Closed-loop biomass

PTC (continued)

- Nature of the incentive
  - This credit provides a 1.5 cent (adjusted for inflation) per kilowatt hour income tax credit for electricity produced from wind, solar, geothermal, biomass (the current rate is available at www.irs.gov/pub/irs-pdf/f8835.pdf).
  - The credit is available for a set term of years determined by the type of resources (for example the wind credit is available for first 10 years of a facilities operation)
  - Generally, the project owner must sell the electricity to an unrelated third party (exceptions--certain biomass and poultry waste faciilties)
- The credit has been quite successful in encouraging wind development

FLIP BUSINESS STRUCTURE MODEL

- Innovative way to capture the value of the PTC and improve project economics
- Allows non-taxable entities such as Indian tribes, to own a significant portion of a wind project, while partnering with an equity investor that can use the federal production tax credits (“PTCs”) generated from the operation of a qualifying wind project
- Must secure a power purchase agreement to sell power to a local utility (or other unrelated third party)
- Under this model, a project limited liability company (“LLC”) is formed to own and operate the wind project
- The LLC owners include the tax equity investor and another entity that includes (or is owned by) the non-taxable entity

FLIP MODEL (continued)

- The Indian tribe (or owner of the resource) typically pays for pre-development expense activities (i.e. permits, wind studies, interconnection and transmission studies)
- The equity investor finances the acquisition of wind turbines and construction of the project (depreciable property)
- The LLC agreement will allocate the wind project’s governance and financial rights between the equity investor and the Indian tribe
- The project can be structured so that the taxable or equity investor has a controlling interest in the project for at least the first 10 years to enable the equity investor to utilize the PTCs or to receive a negotiated rate of return on its investment
- Then, at a date determined by all the participants, ownership “flips” so that Indian tribe has a controlling interest in the project for the remainder of the project’s life

FLIP PROJECT STRUCTURE -- LLC

- Forming a LLC allows the participants to shield their personal and other business assets from liabilities of the project
- Unless it elects otherwise, the LLC will be treated like a partnership for tax purposes
- This tax treatment facilitates use of the PTCs
- Forming a LLC also allows the members to separate governance and financial ownership rights

FLIP MODEL (Tribal Considerations)

- The structure could be a viable model for Indian tribes who own wind energy resources and equity investors interested in partnering in the development of wind projects
- This structure should allow the equity investor to take advantage of federal tax incentives, while providing economic benefits of ownership to the Indian tribe
- However, it must be carefully structured (<u>see</u> the safe harbor requirements in Rev. Proc. 2007-65, 2007-45 I.R.B. 967).

PTC (Tribal Considerations)

- This credit has historically been used to reduce the cost of developing wind resources
- As a tax credit, the incentive is not directly available to public entities, although certain project structures could allow the value of the PTC to be captured
- The “flip structure” may work for some, but IRS guidance leaves a lot of uncertainties and the tribes may not be comfortable with giving the equity investor a controlling interest for the first 10 years
- Lease transactions may result in more net benefits

PTC ALTERNATIVES

- Under the new stimulus bill (ARRA '09), two alternatives to the PTC have been enacted to stimulate renewable energy projects:
  - An investment tax credit ("ITC") in lieu of PTC (30% of cost basis)
  - Treasury grants in lieu of ITC or PTC
- ITC would be subject to same allocation challenges as PTC
- Treasury grant alternative is <u>not</u> applicable to those governmental entities eligible for CREBS (including tribes)

CLEAN RENEWABLE ENERGY BONDS (CREBS)

- This financing mechanism was initially included the Federal Energy Tax Incentives Act of 2005.
- CREBs are available for public entities (tribes, cities, counties, cooperatives) to finance renewable energy projects (www.irs.gov/irb/2006-10_IRB/ar07.html)
- Nature of the Incentive
  - Issuers of CREBS do not pay interest on the bonds
  - A Tribal government (or political subdivision thereof) may be a qualified issuer of a bond
  - Bond holders receive income tax credits in lieu of interest for purchasing a CREB

CREBS (continued)

- Original Allocation: $800 million (Jan 1, 2006- Dec 31, 2007). Over 786 applicants from 40 states applied for $2.5 billion in funds
- 2008 Allocation: $400 million CREBs allocated
  - $250 million to governments
  - $150 million to co-ops
- Emergency Economic Stabilization Act of 2008 authorized an additional $800 million of New CREBs
- American Recovery and Reinvestment Act authorizes up to an additional $1.6 billion in New CREBs ($2.4 B Total)
  - AARA Allocation Formula: No more than 1/3 of total may be allocated to state, local and tribal governments

NEW MARKETS TAX CREDIT

- The New Markets Tax Credit (NMTC) provides a tax credit against federal income taxes for making qualified equity investments in investment vehicles known as Community Development Entities (CDEs)
- Qualified investments must used by CDE to provide investment in low income communities
- Typically used for redevelopment projects, real estate investments and to fund businesses in low-income communities
- Over 40% of all US census tracts qualify for New Markets investments
- In 2008, $3.5 billion in tax credits for use in low-income communities was allocated to 70 organizations
- Tribal allocations
  - National Tribal Development Association received over $30 million in NMTC allocations in prior years
  - Cherokee Nation Businesses received $60 million in NMTC allocations

NMTC (continued)

- Nature of the Incentive:
  - Investor is entitled to claim 39% of the amount of qualified equity investments in credits over a 7 year period
    - First 3 years, the investor receives a tax credit of 5% of the invested amount
    - Final 4 years, the investor receives a credit of 6% percent of the invested amount
- New rule requires a significant level of 2008 allocations to be invested in rural communities, so there is good potential for renewable energy development projects
- Additional Information: www.cdfifund.gov

SUMMARY MATRIX

Entity Type	Formation/ Governance	Sovereign Immunity	Financing	Fed. Tax Treatment
Agencies, Divisions and Instrumentality	Tribal law/ governance and management varies, but often no separate board	Shares Tribe's immunity; can be waived	Bonds and other financing generally available to governments	Not subject to federal income tax
Political Subdivision	Tribal law; must exercise sovereign power; tribal council may oversee	Shares Tribe's immunity; can be waived	Bonds and other financing generally available to governments	Not subject to federal income tax

SUMMARY MATRIX (continued)

Entity Type	Formation/ Governance	Sovereign Immunity	Financing	Fed. Tax Treatment
Section 17 Corporation	Federal charter (DOI); governed by own board; tribe retains certain powers; may hire a professional manager	Shares Tribe's immunity; "sue and be sued" clause should not override or operate as blanket waiver	- Government financing <u>may</u> be available - Tax-exempt bonds, but not CREBs - Private financing should be available	Not subject to federal income tax
State Law Corporation	Created under state law; board of directors and a manager	Not immune, state law determines power to sue and be sued		Subject to federal income tax

SUMMARY MATRIX (continued)

Entity Type	Formation/ Governance	Sovereign Immunity	Financing	Fed. Tax Treatment
Tribal Law Corporation	Tribal Law; board of directors and a CEO or executive director	Depends on how it operates; limits owner liability	Government financing (bonds, CREBs) not available; private financing available	IRS guidance pending
State and Tribal LLCs	State Law or Tribal Law; flexible governance; owners may participate in management	Immunity may not be available	Government financing (bonds, CREBs) not available; private financing available	If more than two owners, taxed like a partnership; if wholly-owned, disregarded as an entity.

WHERE DO WE GO FROM HERE?

- Author Contact Information

Kathleen M. Nilles
Holland & Knight LLP
(202) 457-1815
kathleen.nilles@hklaw.com

Karen J. Atkinson
Native American Contractors Association (NACA)
(202) 349-9845
karen@nativecontractors.org

- Disclaimer: Nothing in this presentation should be construed or relied on as legal or tax advice; rather, it is intended to serve as general guidance on tribal business structures from which better informed requests for legal and tax advice may be formulated.
- Tribal Business Structure Handbook is available for purchase in 2009 at www.nafoa.org/publications.