February 6, 2012

JOINT COMMENTS

[A COMBINED EFFORT FROM TRIBAL GOVERNMENTS, TRIBAL ENTITIES, TRIBAL SERVICE PROVIDERS, AND ASSOCIATIONS]

Submitted Via Federal eRulemaking Portal:
@ www.regulations.gov (IRS-REG-133223-08).

RE: Comments to Advance Notice of Proposed Rule Making
IRS-REG 133223-08
Internal Revenue Code Section 414(d)

Regulations Drafting Group:

The purpose of this letter is to provide comments on the Advance Notice of Proposed Rule Making, IRS-REG 133223-08 (the "Proposed Rule") issued on November 7, 2011 on defining "essential government functions" and "commercial activities" under Internal Revenue Code (the "Code") Section 414(d).

This first set of Joint Comments are the result of a combined effort from the below named tribal governments, tribal entities, tribal service providers, and associations (collectively, the "Tribal Representatives"). Together, the undersigned represent a diverse range of tribal interests in urging several key changes to the Proposed Rule that all of the Tribal Representatives share in common.

Each Tribal Representative also reserves the option to present oral testimony at the upcoming public hearing currently set for July 10, 2012. Those seeking to provide oral testimony will confirm their intent through a separate communication.

Comments:

The undersigned Tribal Representatives contend that the Proposed Rule should be amended in several key respects:

1. The Proposed Rule must be amended to provide greater parity between State and Tribal Governments:

When determining what tribal plans qualify for "governmental status" under Code Section 414(d), tribes should be placed on par with state and local governments. The final rule should minimize the differences between tribal and state governments. This means that it should allow government treatment for revenue generating activities on par with those performed by

state and local governments. The commercial activities restriction should be read narrowly to limit only those activities that are engaged in for private rather than public interests.

While it is true that the statute contains a parenthetical restriction limiting government treatment to "essential government functions" that are not "commercial" in nature, these terms are not defined in the statute or in any legislative history. Thus, these terms can and should be construed in a manner to maximize government treatment and parity between tribes and states. For example, **essential government** function could be read to include any activity that is carried on to preserve or promote tribal self determination, health, education and welfare, including the maintenance of culture and tradition. **Commercial** activities could be read to prohibit only the activities that are carried on for private rather than public interests, and (for parity) not to exclude any revenue generating activity similar in scope, purpose or result to those carried on by state and local governments.

In fact, the United State Supreme Court has ruled that "statutes are to be construed liberally in favor of the Indians with ambiguous provisions interpreted to their benefit " See *Montana v. Blackfeet Tribe*, 471 U.S. 759, 766, 105 S. Ct. 2399, 85 L.Ed.2d 753 (1985)). Thus, the final rule adopted by IRS must be read in favor of government status whenever possible, with all doubt construed in favor of Indian tribes.

The Proposed Rule, however, is completely to the contrary, with almost all possible revenue generating activities construed in favor of commercial status. In doing so, the Proposed Rule does not comport with any sense of parity, the concept and national policy of self-determination, or the above directive from the United States Supreme Court. States and local governments can operate hotels, convention centers, lotteries, stores and golf courses without loss of government status. A rule that would limit tribal revenue generating activities to the sale of souvenirs or a dollar or two at a time for use of a public swimming pool primarily benefitting tribal members is untenable.

The Proposed Rule wholly fails to recognize that: (1) generating revenue for public purposes is an essential government function of Indian tribal governments, and (2) when Indian tribal governments engage in business activities to generate public funds they do so more on par with state and local governments that engage in revenue generating activities than with private entities that do so for private gain.

The Proposed Rule also ignores the fact that tribal governments, unlike private "commercial" enterprises, receive no tax deductions or tax benefits by sponsoring a benefit plan. Establishing a rule that would increase the number of tribal plans subject to the burden of private sector regulation without any corresponding tax benefit is contrary to the foundation of our system of "voluntary" benefits. Tribes do not have to offer benefits, and tribes receive no tax

benefits for doing so. They should not be discouraged, therefore, from offering benefits with a Hobson's choice: offer voluntary benefits and waive government status; eliminate benefits and preserve government status.

The Proposed Rule treats nearly all revenue generating activities engaged in by tribal governments as a "commercial" activity, provides a disincentive for tribes to offer voluntary benefits, and creates a far greater divide between tribal and state governments than is required by the statute at hand.

- The final rule should recognize that generating revenue for public purposes is an essential purpose of tribal government;
- Tribes should be able to engage in any activity that is similar in purpose, scope or result that state or local governments may engage in to generate public funds without jeopardizing tribal government status; and
- The final rule should grant deference to tribal determinations with regard to the essential nature of a government activity and whether or not it is engaged in for commercial or public purposes.

The "commercial" test and presumptions set forth in the Proposed Rule must be brought back within the Supreme Court's directive in the *Blackfeet* case. They are so broad in their present form that almost no tribe will be able to maintain a government status plan. Telling is the following statement from the preamble to the Proposed Rule:

> "If, after applying these rules, an ITG plan sponsor is not certain whether an employee is a government ITG or commercial ITG employee, the ITG may choose to provide coverage for the employee in its commercial ITG plan..."

Simply put, the final rule cannot be used to extinguish government status by attrition, fear and uncertainty. Nor is it reasonable to construe such a narrow set of circumstances that would qualify as "governmental", that the only parenthetical appearance of the term "commercial" ends up negating all of the statutory language that precedes it. The "default" should be government status, not commercial status. The statute was expressly enacted to "clarify" the government treatment of tribes, not to destroy it.

2. The final guidance should adopt a flexible "facts and circumstances" test without relying on the overly restrictive examples or questions stated in the Proposed Rule.

The undersigned agree with use of a "facts and circumstances" test rather than a rigid definition or finite set of examples. A key to any final guidance is that it must be flexible enough to take into account the unique nature of each tribe.

Neither the examples nor the "facts and circumstances" questions contained in the Proposed Rule, however, allow for the flexibility required to take into account the unique nature of each tribe. The final rule should expressly caveat each example confirming that it is not intended to supplant the general test. The final rule should expressly recognize that the result of each example may differ depending on the facts and circumstances particular to a specific tribe.

The questions used in applying the facts and circumstances test should be much broader than those used in the Proposed Rule.

Essential government function test:

In determining whether an activity is an "essential government function", we would suggest the following questions as a framework to begin the facts and circumstances review:

1. Whether the revenues generated by an activity are used for public versus private purposes?
2. Whether the activity is similar (in purpose, scope, or result) to those performed by other governments?
3. Whether the activity is in furtherance of the tribe's stated goals for self-determination, promoting tribal health, education or welfare, or fostering culture and tradition?
4. Whether the activity is supported by a tribal constitution or other tribal laws?

Commercial activities test:

In determining whether an activity is "commercial" in nature, we would suggest the following questions as a framework to begin the facts and circumstances review:

1. Whether revenues from the activity inure to the benefit of the Indian community or to private interests?
2. Whether the activity is subject to federal income tax or not?

We emphasize that the undersigned do not intend the above to be construed as a two part litmus test. It is possible that even a taxable activity or one that has a degree of private benefit can be distinguished from typical "commercial" activity depending on the facts and circumstances at hand. Other factors may also come into play, such as whether the "business" is established to promote tribal employment (including tribal preference) and not necessarily to maximize revenues.

We understand that the "commercial" language as used in the statute could be construed to sweep almost any "business" activity under the private sector rules (which is what the Proposed Rule would do). However, we also understand that the commercial criteria could just as well be read narrowly to preserve government status for all but the most "private" of endeavors. The undersigned believe that the latter is required by rules of statutory construction (reading ambiguities in favor of tribal governments) in the absence of any legislative history to the contrary.

The undersigned contend that "commercial" activities should be limited to those that are done with a profit motive for private gain. The commercial exception should truly be the exception and not the rule, with deference to tribal government status and sovereignty.

A tribal business whose profits are dedicated to public purposes and which engages in revenue generating activity similar to state or local government enterprises should not be treated the same as a "commercial" private enterprise regardless of how "business like" it may appear. State and local governments engage in many activities that could be considered "commercial" in nature. But they remain treated as governmental precisely because they are established to further a government purpose rather than private profit.

Examples reported by the General Accounting Office in 2006 are illustrative:

- From 2000 through 2004, state municipalities issued almost 61 billion dollars in tax exempt bonds for "park and recreation facilities" including theaters, stadiums and arenas.
- There were about 2,400 municipal golf courses reported in 2005, constituting about 15 percent of all golf courses in the United States.
- A significant number of municipal courses were found to have been tied to "resorts or real estate developments".
- More than 300 government owned convention centers and hotels were reported, 11.1 billion dollars of which were identified as having been financed through tax exempt issuances from 2000-2004.
- The GAO report recognized that "all but 2 states have some form of legal gaming [with] 41 states and the District of Columbia providing state lotteries."

Other examples of state and local governments engaging in economic ventures to raise funds for public purposes can be found in almost every community:

- Boat rentals at coastal and lake marinas within state recreation areas and parks;
- Golf at the city owned courses across the country;
- Special events booked at City facilities;
- County and state fairs;
- Football games at public universities and schools that use city and state owned facilities;
- City owned hotel and convention centers;
- Lumber sold from state forest lands;
- state lotteries, state gaming facilities, and state revenue sharing with tribal entities;
- State liquor stores;

All of the above activities could be called "commercial" but for the fact that the revenues they generate inure to the benefit of public rather than private interests.

3. The final rule should reject the examples of Notice 2006-89 and not extend amendment restrictions that have long outlasted their purpose.

The Proposed Rule continues the artificial categories set forth in Notice 2006-89 as "examples" of commercial activity (casinos, hotels, service stations, convenience stores and marinas) as if they were supported by the force of law or legislative history. They are not. There is no evidence in the statute itself that casinos, hotels, service stations, convenience stores or marinas were intended to be categorically treated as "commercial" activities. There was no floor debate addressing the issue or the categories in Notice 2006-89. Nor did a single bill leading up to the Pension Protection Act contain such examples. These categories were established solely by the Joint Committee on Taxation with no input from tribes and no consultation as required by Executive Order 13175. If states can conduct lotteries to raise public funds without question, the categories set forth in Notice 2006-89 must fall.

We also note the inherent flaw in using any "activity" examples to "deem" commercial status. The examples presume that commercial status can be decided by looking at "covered activities" in isolation. However, this is not how distinctions are drawn in real life. There are many for-profit, non-profit, and government status entities that perform the same basic set of activities. For example, public schools and private schools; government hospitals and private hospitals. It is not the "activity" that makes something "commercial" or "governmental"; it is the existence of private benefit and profit motive versus public benefit and public service that is key.

Finally, the Proposed Rule also purports to extend restrictions on the ability of tribal employers to amend their plans. These restrictions were misguided from the start and violate any sense of deference or government-to-government protocol. The restriction is based on the apparent fear that tribal governments will cut back benefits for commercial plans more severely than to their government status plans. First, there is no evidence that tribal governments are any less fair than other governments when it comes to plan design. Second, even if tribal governments wanted to provide more lucrative benefits for government workers than for "commercial" workers, such a decision is for the tribal government to make, not the IRS. The IRS does not second guess state and local governments when they elect to pay higher benefits with often corresponding lower wages than the private sector. These are decisions that are simply no business of the IRS.

We also note that the amendment restrictions were initially posed as a condition to receive "temporary" good faith relief pending the promise of future guidance. That "temporary" condition has now lasted for more than a half decade, during an economic downturn when other employers (both government and private sector) have been forced to cut back and adjust benefits to survive. These restrictions discriminate against tribal employers, fly in the face of tribal sovereignty, and must be eliminated.

4. The final rule must not require tribes to split employees between two different plans at the same time.

The Proposed rule purports to require employees with split service between government and commercial entities to split participation between both the tribe's commercial and government plans. This is unworkable and far too costly. The difficulty and burden in maintaining both government status and commercial status plans at the same time is unprecedented. In fact, the Proposed Rule does not even attempt to address the substantive compliance rules, confirming instead that

> "these proposed regulations do not address the rules under which, for purposes of sections 401, 408(k), 408(p), 410, 411, 415 and 416, all employees of all corporations that are members of a controlled group of corporations are treated as employed by a single employer for purposes of these controlled group rules."

We understand the difficulty in providing substantive guidance and why, after six years, there remain more questions than answers. However, it is not acceptable to forge full steam ahead with a rule that would favor more plan splits and more "shared" status employees without addressing the substantive fallout.

The final rule cannot avoid guidance on control group issues and then compound compliance difficulty for tribes by requiring more employees to split between more plans. The fact is that tribal governments are not "corporations." None of the above statutes purport to apply control group testing to tribal governments and there is certainly no legislative history indicating any intent to do so. Rather than postponing guidance again after the six years tribes have already waited, IRS should stop trying to fit a square peg in a round hole and simply confirm that the control group testing requirements do not and will not apply.

As for classifying employees between tribal government and commercial plans, it should be left up to the governing bodies of each tribe to establish a single employer plan for each employee class based on the majority of assigned duties.

5. Tribal entities should be granted a moratorium on compliance requirements pending final guidance.

The undersigned reiterate comments from tribes and tribal organizations from across the country when the Pension Protection Act (the "PPA") was first enacted, requesting a moratorium on enforcement actions under the PPA until after tribes are provided final guidance and time to comply. The IRS granted a similar moratorium to state and local governments that lasted two decades pending congressional relief. The "transitional" relief under Notice 2006-89 and Notice 2007-67 does not provide sufficient guidance or relief. In fact, that "relief" has resulted in many tribes abandoning government status because of the extended periods of uncertainty and added cost of compliance. Having to file 5500s, for example, without any guidance for CPA firms on control group testing, or having to file IRS determination letter applications before plan "splits" are even required, have all proven costly.

After six years of waiting, the Proposed Rule does not address control group requirements or any of the technical and compliance difficulties facing tribes under the PPA. These are exactly the circumstances that state and local governments faced in the 1980s and 1990s. Tribes should be granted an express moratorium and relief. The relief should be from all compliance amendments, reporting requirements (5500s), control group testing, 401(b) remedial amendment relief and other amendment deadlines pending the issuance of final guidance under the PPA. Tribes should be afforded a good faith standard with no design restrictions or artificial categories for presuming commercial status.

6. The final rule should recognize consultation rights under Executive Order 13175.

The Proposed Rule contains a statement that it does not "have substantial direct effects with respect to the Federal government and Indian tribes" and that it does not implicate consultation under Executive Order 13175.

The undersigned urge a broad reading of consultation rights under Executive Order 13175, including a provision in the final rule allowing individual consultation and waiver requests to resolve conflicts between a tribe and IRS on the proper classification of a tribal entity or employee.

The final rule should expressly recognize individual consultation rights for tribes that may disagree on the characterization of an individual entity and the availability of administrative waiver requests as contemplated in Executive Order 13175, Section 6, on an individual basis.

7. Administrative Correction Should be Liberally Construed.

The Proposed Rule requests comment on the availability of administrative correction programs for errors related to government status plans. The undersigned contend that administrative relief should be construed liberally in favor of tribal governments consistent with the "government-to-government" relation between the federal and tribal governments.

8. The final rule should reflect recent recommendations from Treasury and the IRS Advisory Committee on Taxation.

The undersigned urge the final rule to reflect recommendations by the IRS Advisory Committee on Taxation to grant relief from PPA requirements pending final guidance, and to exempt tribes from the control group testing requirements. The undersigned also urge the final rule to reflect Treasury's recent report on tax exempt bonds in which it recommends elimination of the essential government function test.

RESPECTFULLY SUBMITTED:*

AMERIND
Blue Lake Rancheria
The Chickasaw Nation
The Coquille Tribe
Eastern Band of the Cherokee Nation
Gregg Fendley Benefits
Gila River Health Care
Grand Portage Reservation Tribal Council
HealthSmart / TribalCare
Hoopa Valley Tribe
Hopi Tribal Pension Committee
The Hualapai Tribe
[The Hualapai Tribe is also submitting, in a separate filing, additional comments based on circumstances specific to its government]
Morongo Band of Mission Indians
Navajo Tribal Utility Authority
Plan Sponsor Council of America (PSCA)
RCG Plan Administration, LLC
Redding Rancheria
REDW LLC
Salt River Pima-Maricopa Indian Community
[The Salt River Pima-Maricopa Indian Community is also submitting, in a separate filing, comments based on circumstances specific to its government]
Sovereign Benefits Group, Inc
Sovereign Finance LLC
The Suquamish Tribe
The Tulalip Tribes
[The Tulalip Tribes is also submitting, in a separate filing, additional comments based on circumstances specific to the legal and organizational structure of the Tulalip Tribes and governmental entities in the Pacific Northwest region]
Ute Mountain Ute Tribe
Yavapai Apache Nation
Yoder & Langford, P.C.

* The undersigned reserve the right to submit and join in a Second Supplemental Set of Joint Comments or individual comments under the extended comment period [as announced in Federal Register Volume 77, Number 23, February 3, 2012]