JOINT COMMENTS OF

THE PROFIT SHARING /401(k) COUNCIL OF AMERICA
and
YODER & LANGFORD, P.C.

January 22, 2007
submitted electronically

RE: Comments to Notice 2006-89
Transition Relief for Indian Tribal Government Plans
Definition of "commercial" employee under Code Section 414(d)

This letter is provided in response to the request for comments appearing in Notice 2006-89 (the "Request for Comment") with regard to the treatment of Indian tribal governments as governmental employers under Internal Revenue Code (the "Code") Section 414(d), as amended by the Section 906 of the Pension Protection Act of 2006 (the "PPA").

The Profit Sharing / 401(k) Council of America (PSCA), established in 1947, is a national non-profit association of 1,200 companies and their 6 million employees that advocates increased retirement security through profit sharing, 401(k), and related defined contribution programs to federal policymakers and provides practical assistance on profit sharing and 401(k) plan design, administration, investment, compliance, and communication to its members. PSCA's services are tailored to meet the needs of both large and small companies, with members ranging in size from Fortune 100 firms to small entrepreneurial businesses.

Yoder & Langford, P.C. represents more than 30 Indian tribal governments across the country from New York to California solely on issues of federal taxation, employee benefits, and employment law. The firm has also worked with tribes and tribal organizations for the past 17 years on efforts to secure better regulatory and legislative guidance for tribal government entities.

The comments provided herein focus on who will be considered a "commercial" employee under Code Section 414(d) and the relief tribal governments need at this time in order to implement those operational changes needed in order to comply with the new commercial / governmental distinction among tribal plans.

Summary of Comments:

The comments urged herein, and as more fully supported below, can be summarized as follows:

1. Whether an activity is "commercial" should be determined on a facts and circumstances basis.

- The regulations should establish key factors to be considered:

(1) the historic functions performed by the tribal government;

(2) the tribe's role as defined in its Constitution, Bylaws, Ordinances, Resolutions, Judicial decisions, customs and traditions;
(3) the functions carried on by other governmental employers, including the federal government, states, counties, cities and other local governments;
(4) the use of revenues generated by activities in question (whether inuring to the benefit of the tribe and the provision of public services, or whether inuring to private interests);
(5) whether the entity or division is treated as a non-profit or for-profit entity for tax or other purposes; and
(6) whether the function is funded through the federal or state governments, such as those carried out under public law 638, the Indian Self Determination Education and Assistance Act.

- The regulations should not adopt the restrictive commercial examples set forth in the Joint Tax Committee's explanation to the PPA and as incorporated into Notice 2006-89.

2. The proposed regulations should clarify the treatment of tribal entities under the Code Section 414(b), (c) and (m) control group tests:

- The Code Section 414 control group definitions should not be expanded to include tribal entities that do not fit within the current statutory definitions.
- To the extent control group testing is applied to tribal entities, the proposed regulations should expand the Qualified Separate Line of Business testing exceptions to accommodate structure issues unique to tribal governments.
- The new regulations should provide relief to allow for the transfer of employees and benefits among different tribal entities.
- The new Guidance should clarify that "commercial" entities may exclude government employees for purposes of coverage and minimum participation tests.

3. The proposed regulations should clarify that Section 906 of the PPA was not intended to disrupt core sovereignty rights over domestic relations.

- Without such clarification, some tribal members pursuing a QDRO may need to have their marriages or divorces governed by state law rather than tribal law if one of the spouses works for a "commercial" tribal entity.

4. The new rules should clarify compensation related issues for shared employees, participation in tribal plans by elected tribal officials and by those tribal members who receive tax exempt treaty rights related income.

- Revenue Ruling 59-354.
- Code Section 7873.

5. New Guidance should clarify that all tribal entity plans that are split or converted from a Code Section 414(d) plan by the transitional relief date (currently September 30, 2007) are relieved from the "A Cycle" determination letter deadlines.

6. Guidance should provide relief to tribal employers who adopt safe harbor plans during the transition period.

7. Guidance should confirm that plans that are under VCP review for years prior to the PPA effective date are entitled to rely on Code Section 414(d) status.

8. The Guidance should provide additional time for tribal governments to make those changes necessary for compliance with the new rules.

9. Additional time for comment and consultation with tribes on a government-to-government basis under Executive Order 13175 is needed before proposed regulations are published.

Comments:

1. **Whether an activity is "commercial" should be determined on a facts and circumstances basis**.

   (a) There is no statutory definition or legislative history defining the term "commercial". Thus, the term must be construed in a light favorable to tribal governments.

The term "commercial" is not defined in the PPA or anywhere else in the Internal Revenue Code. Nor was there any discussion of its use in the legislative history to the PPA[1]. The "commercial" employee distinction did not appear in any of the House or Senate versions of the tribal pension reform bills[2]. Its only appearance is found in the final draft that was being considered by the conference committee. The conference committee did not complete its review before the vote was taken, and a final conference report was not published. Thus, there is no indication from Congress what was meant by use of that term.

In the absence of a statutory definition or legislative history, one must revert to judicial rules of construction. In this case, the term "commercial" is, by its very nature, ambiguous. It could be read broadly to encompass any revenue generating activity. Alternatively, it could just as reasonably be read to include only those activities engaged in on a "for profit" basis for the benefit of private shareholders. As noted by the United States Supreme Court:

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[1] The Joint Committee on Taxation published an explanation of the Pension Protection Act, providing examples of what that committee thought to be "commercial" and non-commercial. However, that explanation does not necessarily reflect Congressional intent.

[2] See, for example, S 673 (introduced March 17, 2005) and HR 331 (introduced January 25, 2005).

"statutes are to be construed liberally in favor of the Indians with ambiguous provisions interpreted to their benefit "

Montana v. Blackfeet Tribe, 471 U.S. 759, 766, 105 S.Ct. 2399, 85 L.Ed.2d 753 (1985)).

Thus, we urge the Service to adopt a flexible approach to determining whether an activity will be treated as "commercial", and to allow deference to the elected tribal bodies in applying key factors relevant to that inquiry.

(b) The regulations should not adopt the commercial examples set forth in the Joint Tax Committee's explanation to the PPA, and as incorporated into Notice 2006-89.

Notice 2006-89 incorporated several "commercial" examples offered by the Joint Committee on Taxation. We urge the Service to reject such a categorical approach. There are some entities that perform the same basic function, some of which may be "commercial" and some of which may be "non-commercial" in nature. There are public school systems in every state (and within most tribal governments) that cannot be considered "commercial" activities. By the same token, there are certainly private schools at every educational level that are surely commercial in nature. There are also "for profit" "commercial" hospitals, and others that provide hospital care pursuant to Code Section 501(c)(3).

What makes something "commercial", therefore, does not always depend on the function that is being performed.

(c) The regulations should recognize key factors to be considered:

Instead of focusing on what the entity does (education, tourism, or health care), we urge the Service to focus on what purpose the entity serves (public *versus* private needs). We would encourage a rule that would consider factors such as the following:

(1) the historic functions performed by the tribal government;
(2) the tribe's role as defined in its Constitution, Bylaws, Ordinances, Resolutions, Judicial decisions, customs and traditions;
(3) the functions carried on by other governmental employers, including the federal government, states, counties, cities and other local governments;
(4) the use of revenues generated by activities in question (whether inuring to the benefit of the tribe and the provision of public services, or whether inuring to private interests);
(5) whether the entity or division is treated as a non-profit or for-profit entity for tax or other purposes; and
(6) whether the function is funded through the federal or state governments, such as those carried out under public law 638, the Indian Self Determination Education and Assistance Act .

We recognize that this analysis could result in the exclusion of gaming facilities from those entities treated as "commercial" so long as the gaming facility restricted revenues to public uses. Under this analysis, however, it is important to recognize that many forms of government, in addition to tribal governments, engage in activities that, in isolation, could also be viewed as "commercial. What makes them "governmental" is not the activity being performed, but the purpose that those activities serve - - - whether the funds inure to public or private interests. Examples appearing in last year's General Accounting Office Report 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."

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 the Antioch Marina along the San Joaquin River in California (owned and operated by the City of Antioch);
- Golf at the Riverside Municipal Golf Course (one of three golf courses owned by the City of Fresno);
- Special events booked at the Huntington Central Park (the largest city owned and operated regional park in Orange County);
- The annual USC / Notre Dame Football game held at the Los Angeles Memorial Coliseum (owned by the City of Los Angeles, and once home to several professional sports franchises);
- Reservations in a city owned hotel or convention center, like those in Houston or Austin, Texas;
- Lumber purchases from the State of Washington or Wisconsin (who proudly "market forest products" to fund local government services and sustain statewide economies);
- "Big Pick" lottery tickets in Arizona;
- Skiing at the Winter Park Ski Resort & Lodge (owned by the City of Denver);
- Liquor purchases from the City owned liquor store in Mantorville Minnesota, Pennsylvania or Delaware;
- City Council meetings in Pittsburgh (which last year endorsed a plan to bid on one of Pennsylvania's coveted gaming licenses;
- Public debates over Mayor Daley's recent bid for a city owned land based Casino in Chicago;

- Watching rescues on the evening news, from a city fire truck just purchased with funds received from tribal gaming revenue share agreements in California, Arizona, Michigan, Connecticut, New Mexico, New York or Wisconsin.

Guidance should confirm that tribal government plan participants can engage in economic enterprise activities, and will not be treated as "commercial" employees, so long as the enterprise is operated to raise general revenues for public rather than private purposes.

(d) Guidance is needed with regard to shared employees.

Once it is determined what functions are "commercial", tribes will also need guidance with regard to those "government" employees that provide services to "commercial" enterprises as well. For example, the tribal accounting staff may process payroll for both the "government" and a tribal owned "commercial" entity. A tribal finance director may advise on "commercial" matters. The attorney general's office or general counsel may advise on "commercial" matters.

A mechanical "percentage" test will not work, in our view, as the percentage of "commercial" services will vary in most cases depending on particular activities over time. The general counsel, for example, may spend almost all of his or her time for a month or a year on contract negotiations for a commercial venture, and then spend most of the next year largely on tribal water rights. Changing an employee's plan status based on what he or she may be doing at a given moment would be unworkable. Rather, we would like to see presumptive determinations, left to the governing tribal councils, as to whether the employee is serving the government interests in a non-commercial manner.

(e) Guidance should be flexible enough to reflect the fact that "essential" government functions and "commercial" activities may change over time.

Any rule advanced at this time should be flexible enough to reflect that what is an essential government function or considered "commercial" today, may change over time. We encourage the Service to reflect on similar attempts to define these terms in other contexts before making a rule under the PPA. At one time, for example, state governments faced a similar predicament when courts attempted to define state tax immunity with reference to what the courts deemed to be "essential", "ordinary" "traditional" , "strictly governmental" and "customary" functions[3]. These distinctions were first drawn in *South Carolina v. United States,* 199 U.S. 437, 26 S.Ct. 110, 50 L.Ed. 261 (1905), wherein the Supreme Court announced a ruling, now rejected, that state tax immunity would be recognized only when a state was performing "strictly governmental" functions and not when carrying out "ordinary private business." 199 U.S., at 451, 461, 26 S.Ct., at 112, 116. While the Supreme Court continued to apply that distinction for the next 40 years, it later recognized that "at no time during that period did the Court develop a consistent formulation of the kinds of governmental functions that were entitled to immunity." *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528, 541-542 (1985). In commenting on the

[3] See *Flint v. Stone Tracy Co.,* 220 U.S. 107, 172, 31 S.Ct. 342, 357, 55 L.Ed. 389 (1911) ("essential"); *Helvering v. Therrell,* 303 U.S. 218, 225, 58 S.Ct. 539, 543, 82 L.Ed. 758 (1938) (same); *Helvering v. Powers,* 293 U.S. 214, 225, 55 S.Ct. 171, 173, 79 L.Ed. 291 (1934) ("usual"); *United States v. California,* 297 U.S. 175, 185, 56 S.Ct. 421, 424, 80 L.Ed. 567 (1936) ("activities in which the states have traditionally engaged"); *South Carolina v. United States,* 199 U.S. 437, 461, 26 S.Ct. 110, 116, 50 L.Ed. 261 (1905) ("strictly governmental").

development and fall of the "essential governmental function" test in that context, the Supreme Court, in *Garcia,* noted as follows:

> "[t]he Court identified the protected functions at various times as 'essential,' 'usual,' 'traditional,' or 'strictly governmental' [reflecting] an inability to specify precisely what aspects of a governmental function made it necessary to the 'unimpaired existence' of the States. Indeed, the Court ultimately chose 'not, by an attempt to formulate any general test, [to] risk embarrassing the decision of cases [concerning] activities of a different kind which may arise in the future.'"

Id. (quoting from *Brush v. Commissioner,* 300 U.S., at 365, 57 S.Ct., at 498 (internal citations omitted). In *Garcia*, the Supreme Court went further in explaining the inherent problems in trying to distinguish "governmental" from "business" activities conducted by governments:

> "If these tax-immunity cases had any common thread, it was in the attempt to distinguish between 'governmental' and 'proprietary' functions. To say that the distinction between 'governmental' and 'proprietary' proved to be stable, however, would be something of an overstatement. In 1911, for example, the Court declared that the provision of a municipal water supply 'is no part of the essential governmental functions of a State'' *Flint v. Stone Tracy Co.*, 220 U.S. 107, 172, 31 S.Ct. 342, 357, 55 L.Ed. 389. Twenty-six years later, without any intervening change in the applicable legal standards, the Court simply rejected its earlier position and decided that the provision of a municipal water supply *was* immune from federal taxation as an essential governmental function, even though municipal water-works long had been operated for profit by private industry. *Brush v. Commissioner,* 300 U.S., at 370-373, 57 S.Ct., at 500-502. At the same time that the Court was holding a municipal water supply to be immune from federal taxes, it had held that a state-run commuter rail system was *not* immune. *Helvering v. Powers,* 293 U.S. 214, 55 S.Ct. 171, 79 L.Ed. 291 (1934). Justice Black, in *Helvering v. Gerhardt,* 304 U.S. 405, 427, 58 S.Ct. 969, 978, 82 L.Ed. 1427 (1938), was moved to observe: 'An implied constitutional distinction which taxes income of an officer of a state-operated transportation system and exempts income of the manager of a municipal water works system manifests the uncertainty created by the 'essential' and 'non-essential' test' (concurring opinion). **It was this uncertainty and instability that led the Court shortly thereafter**, in *New York v. United States,* 326 U.S. 572, 66 S.Ct. 310, 90 L.Ed. 326 (1946), **unanimously to conclude that the distinction between "governmental" and "proprietary" functions was "untenable" and must be abandoned**."

Id. The Court further noted that:

> "The distinction the Court discarded as unworkable in the field of tax immunity has proved no more fruitful in the field of regulatory immunity under the Commerce Clause. Neither do any of the alternative standards that might be employed to distinguish between protected and unprotected governmental functions appear manageable. **We rejected the possibility of making immunity turn on a purely historical standard of "tradition"** in *Long Island,* and properly so. **The most obvious defect** of a historical approach to state

> immunity **is that it prevents a court from accommodating changes in the historical functions of States, changes that have resulted in a number of once-private functions like education being assumed by the States and their subdivisions.** At the same time, the only apparent virtue of a rigorous historical standard, namely, its promise of a reasonably objective measure for state immunity, is illusory. **Reliance on history as an organizing principle results in line-drawing of the most arbitrary sort**; the genesis of state governmental functions stretches over a historical continuum from before the Revolution to the present, and courts would have to decide by fiat precisely how longstanding a pattern of state involvement had to be for federal regulatory authority to be defeated."
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> **"Indeed, the "traditional" nature of a particular governmental function can be a matter of historical nearsightedness; today's self-evidently "traditional" function is often yesterday's suspect innovation**."

Garcia at 543, 544 fn 9 (emphasis added).

After citing numerous examples of failed attempts to regulate state governments based upon a notion of what is "essential" "historical", "necessary", or "proprietary", the Court noted the following passage that we now assert should be reflected in the regulatory project at hand:

> **"[T]here is a more fundamental problem at work here, a problem that explains why the Court was never able to provide a basis for the governmental/proprietary distinction in the intergovernmental tax-immunity cases and why an attempt to draw similar distinctions with respect to federal regulatory authority [] is unlikely to succeed regardless of how the distinctions are phrased. The problem is that neither the governmental/proprietary distinction nor any other that purports to separate out important governmental functions can be faithful to the role of federalism in a democratic society. The essence of our federal system is that within the realm of authority left open to them under the Constitution, the States [and tribal governments] must be equally free to engage in any activity that their citizens choose for the common weal, no matter how unorthodox or unnecessary anyone else-including the judiciary-deems state [or tribal] involvement to be. Any rule [] that looks to the "traditional," "integral," or "necessary" nature of governmental functions inevitably invites an unelected [body] to make decisions about which state [or tribal] policies it favors and which ones it dislikes. . . There is not, and there cannot be, any unchanging line of demarcation between essential and non-essential governmental functions. Many governmental functions of today have at some time in the past been non-governmental. The genius of our government provides that, within the sphere of constitutional action, the people-acting not through the courts but through their elected legislative representatives-have the power to determine as conditions demand, what services and functions the public welfare requires."**

Garcia at 545, 546 (emphasis added). From these lessons noted by the Supreme Court in *Garcia*, we urge (1) that guidance be drafted in a manner designed to accommodate flexibility, and (2) that guidance not

restrict (by example or otherwise) tribal government plan participant activities more than is expressly required by the statute itself.

2. <u>Guidance should clarify the treatment of tribal entities under the Code Section 414(b), (c) and (m) control group tests</u>.

Once it is determined which plans will be treated as "commercial" plans and which will be treated as "governmental" plans, practitioners and plan sponsors will need to know how separate "commercial" entities of the same tribal government are to be treated for control group testing purposes.

(a) Guidance should confirm that control group tests do not apply.

Code Section 414(b), 414(c) and 414(m) define control groups, common control and affiliated service groups with reference to corporate share ownership and profits interests. These testing statutes do not reference any government owned entities. Nor is there an indication in the legislative history to any of the foregoing statutes of an intent to apply those requirements to tribal government entities.

As a general matter, tribal owned entities do not issue stock. Most are structured under tribal charters, through tribal resolution, through tribal ordinance, through tribal non-stock corporate codes, or through federal Section 17 corporate charters. To the extent a tribal entity does not expressly fit within the definition of a control group under Code Section 414(b), Guidance should clarify that those provisions will not be read more expansively than the statute requires. Under the statutory construction principals of *Montana v. Blackfeet Tribe*, 471 U.S. 759, 766, 105 S.Ct. 2399, 85 L.Ed.2d 753 (1985)), the control group testing requirements must be "construed liberally in favor of" tribal governments.

Code Section 414(c) picks up certain other "trades or businesses" "whether or not incorporated". However, the statute vests in the Secretary discretion to promulgate regulations identifying which "other" non-incorporated entities are to be included - - - based on principals "similar to" those applied to corporations.

The regulations prescribed under Code Section 414(c) do not mention tribal governments. We urge the Service to issue guidance confirming, therefore, that these control group concepts will not be applied to tribal owned entities in a manner not expressly required by the statute itself.

(b) Current control group rules, if applied, would cause hardship for small tribal entities.

If coverage tests (under Code Section 410(b)) must be performed on a control group basis, many small tribal plans will need to be terminated or merged into other commercial plans. Ironically, these testing requirements do not generally impact big Casino plans, which in most cases have many more employees than other types of tribal entities. It hits the small traditional and cultural entities the hardest - - - entities that in many cases cannot afford to offer the same benefits, rights and features as offered under the larger tribal entity plans.

For example, a farming enterprise with 20 employees and a single HCE[4] would have great difficulty passing the Code Section 410(b) coverage test when aggregated with a Casino plan that has 2,000 non-highly compensated employees even if the Casino plan has only one HCE[5]. In that example (which is not uncommon), it is obvious that neither plan is set up to discriminate in favor of highly compensated employees. However, unlike large corporate employers who can take advantage of the Qualified Separate Line of Business Rules[6] and have subsidiaries tested on a separate employer basis, many tribes have historically maintained a large number of very small entities. For example, some tribes have numerous revenue generating enterprises[7] that would never be brought together for "business" reasons under a typical "corporate" model:

- Housing authorities (can engage in tribal housing rentals and maintenance),
- Utility authorities (several tribes own and operate utilities out of necessity, which are sold to members on a usage basis. tribal enterprises may also become "customers" of a tribal utility authority),
- Convenience stores (many tribes in remote areas have access only to tribal owned stores for groceries and other household items),
- Gas stations (many of which are in extremely remote areas owned by the tribal government as a matter of necessity),
- Game and fish departments (fishing licenses, fish hatcheries and sales to state game and fish departments for stocking) ,
- Natural resource and recreation departments (cabin rentals, camping and hunting permits)
- Waste management services (trash collection),
- Cattle ranching and support activities (often engaged in as a means to retain culture and tradition rather than as a means to make "profits"),
- Transportation services (tribal owned van services to transport members and seniors located in remote areas),
- Tribal hospitals (which operate under the Indian Self Determination and Education Assistance Act on behalf of the federal Indian Health Services, and are encouraged to reduce federal budget needs through third party billings).
- Job training and apprentice programs funded with federal and state grants to encourage employment opportunities on tribal reservations,
- Mining services (tribal owned operations managing tribal land minerals, oil and coal),
- Tribal land management enterprises (charged with overseeing tribal land rentals and industrial properties),

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[4] As used herein, the term "HCE" refers to a "highly compensated employee" under Code Section 414(q).

[5] In that example, the farming plan (which covers 100% of its own employees) would benefit 50% of all HCEs within the control group, but only nine tenths of a percent of the non HCEs when counting the entire control group. The farming operation is also too small to be treated as a separate entity for testing purposes under the qualified separate line of business testing requirements of Code Section 414(r). Thus, a tribe in that example must either (1) terminate its small employer plans, or (2) merge them into large enterprise plans that may be more costly (with match or profit sharing components that a small enterprise often cannot afford). In many cases there are also practical constraints preventing small tribal entities from participating in a large enterprise plan.

[6] The "QSLOB" rules are found at Code Section 414(r).

[7] By inclusion in this list we do not imply that these entities should be treated as "commercial". To the contrary, we would urge the Service to confirm that each such entity is non-commercial in nature, performing various public functions for the benefit of the tribal government as a whole.

- Tribal owned Emergency Medical Service enterprises that contract to provide medical services to both tribal and non-tribal enterprises, localities, and events,
- Tribal consortiums which have banded together to provide various services (such as medical services and risk retention /risk pool services) that tribes may be too small individually to obtain, and that private sector entities lack sufficient economic incentives to provide.
- Sand and gravel operations (selling and processing gravel and cement mined from tribal lands,
- Tribal owned halls and pavilions (rented to tribal members to perform ceremonies),
- Fishing rights related entities (harvesting and processing of fish pursuant to treaty rights and recognized under Code Section 7873)
- Wood and forest services (selling trees and lumber harvested from tribal lands and from managing tribal forests),
- Pottery and Native arts enterprises (established by tribes to maintain their culture and traditions),
- Hotels, golf courses, gaming facilities, and marinas which expressly restrict the use of all proceeds to public purposes.

As with the traditional collection of tax, all of the above have some "revenue" component to their operations. Most of them are often staffed with less than 50 employees each, meaning that they cannot be treated as "qualified separate lines of business" if the control group tests of Code Section 414 apply. Moreover, each entity may have separate payrolls, separate revenue flows, and separate employee demographics making the "one size fits all" approach untenable.

(c) To the extent control group testing is applied to tribal entities, guidance should be promulgated to expand the Qualified Separate Line of Business testing exceptions to accommodate structure issues unique to tribal governments.

As noted above, tribal entities are not commonly structured as a stock corporation. Often, an enterprise is merely set up by Council resolution with no separate legal barrier between it and the tribal government itself. Ultimately, the control of most tribal entities can be traced back to either the elected governing council or to the enrolled membership, depending on each tribal constitution which will vary by tribe. In some cases, the elected governing council will oversee management of each enterprise under the tribe[8].

If control group rules are applied to tribal entities, the QSLOB regulations should be amended to ensure that tribes will not fail the "common management" tests simply due to their tribal constitutional structure. Given that the 50 employee rule is statutory, we would also encourage the Secretary to consider special rules allowing, for example, small tribal entities, in combination, to be treated as a QSLOB.

(d) Guidance is needed with regard to the transfer of employees and benefits among different tribal entities.

[8] The vast differences in tribal government structure make it impossible to generalize. Some tribes are "treaty" governed tribes. Some are not. Some have "BIA form constitutions" and charters that have not been amended for half a century. Some have constitutions very similar to state or federal models. This extreme difference in tribal structures is indicative of why the Service should be cautious in applying control group rules in this context at all. It also exemplifies the need for individual consultation with tribes before implementing such broad based concepts in this area.

Many tribes have employees who transfer between different tribal entities on a frequent basis, much more so than in "corporate America". It is also not uncommon for a "government" employee to work weekends at a tribal "commercial" entity. This presents several problems for an employer that is now subject to two sets of rules (government sector and private sector) at the same time depending on what function an employee may be performing at any given moment.

One practical problem, for example, has to do with the 401(k) distribution event rules. If the entities are treated as a "single employer" there would not appear to be a distribution event when an employee leaves one tribal entity for employment at another. Now that most tribal entities will have to maintain separate plans for their government and "commercial" employees, we would urge guidance that would allow employees to transfer their 401(k) benefits to a successor entity within the tribal control group. Without such transfer rights, the "separate plan" structure required by the PPA may create undue hardship for individual employees wanting to take plan plans or hardship distributions under the plan(s), and would create multiple accounts and recordkeeping burdens that would be confusing to employees and costly to employers.

There are also a number of other compliance issues which must be confronted as a result of the same employer being subject to two sets of rules. The commercial plan, for example, will be subject to ERISA service crediting rules and Code Section 410(b). The government sector plan would not. When an employee transfers between "commercial" and "government" employment, someone will need to know what service must be counted and retained. May service with a government entity be excluded? May the government entity exclude "commercial service"? What about shared employees?

3. <u>The proposed regulations should clarify that Section 906 of the PPA was not intended to disrupt core sovereignty rights over domestic relations</u>.

If a statute affects tribal sovereignty rights or treaty rights, there must be "clear and reliable evidence from the statute or from the legislative history that Congress intended to infringe upon tribal rights". *See Minnesota v. Mille Lacs Band of Chippewa Indians*, 526 U.S. 172, 202 (1999); *see also United States v. Dion*, 476 U.S. 734,739 (1986).

The PPA could be construed to interfere with several core rights of sovereignty that were clearly not contemplated or intended. For example, Code Section 414(p) (which applies to "commercial" plans) restricts the division of pension assets upon divorce to those instances where a qualified domestic relations order (a "QDRO") is issued. Unfortunately, Code Section 414(p)(1)(B) requires such an order to be issued "pursuant to a State domestic relations law".

There is no evidence that Congress intended to disenfranchise tribal sovereignty rights over tribal domestic relations. In fact there is no legislative history at all indicating why the final statutory language was modified in manner that now requires tribal governments to separate their plans between governmental plans and commercial plans. Given the lack of such an expressed intent, the statute cannot be construed to take these core sovereignty rights away.

Guidance should be issued which clarifies that a QDRO may be issued under state or tribal domestic relations law (in state or tribal court) as applicable. The ERISA implications of sovereignty

waivers are even more pervasive, potentially disenfranchising the tribal government of its judiciary system, with most benefit claims granting claimants concurrent jurisdiction in state and federal court[9].

4. <u>Guidance should clarify unique "compensation" rules that will be needed to coordinate shared employees, participation in tribal plans by elected tribal officials and participation by those individuals who receive tax exempt treaty rights related income</u>.

Many tribal governments across the country reserved specific treaty rights related to fishing, fish harvesting, and fish processing. In fact, Code Section 7873 expressly exempts qualified tribal members from income tax on their fishing rights related income. If these treaty rights related "businesses" are treated as "commercial" entities, they will be subject to ERISA and they will be subject to the 401(k), (m) and 410(b) tests. A pre-tax 401(k) plan does not work well for "tax exempt" income[10]. Moreover, some of these fishing rights related employees receive only a portion of their pay from qualifying tax exempt activities and are, therefore, mixed or shared employees. We would need guidance, then, as to how these employees should be treated.

Along a similar line, elected tribal council officials are, under Revenue Ruling 59-354, not to be treated as "employees" for wage purposes. Under that ruling, they are not subject to FICA, even though they are subject to income tax. The Indian Tribal Government division of the IRS has advised tribes throughout the country to report these "non-wages" as "W-2" wages. We would urge a resolution of this issue with any guidance on how the definition of compensation will need to be modified to reflect private sector testing of tribal entity plans.

Guidance should also clarify that compensation for a shared employee or an employee who transfers mid year between a tribal "government" and a tribal "commercial" entity need not be aggregated for benefit purposes. Guidance should also clarify whether both governmental and non-governmental wages will be considered in aggregate for HCE purpose.

5. <u>New Guidance should clarify that all tribal entity plans that are split or converted from a Code Section 414(d) plan by the transitional relief date (currently September 30, 2007) are relieved from the "A Cycle" determination letter deadlines.</u>

Under the new determination letter filing schedule (see Revenue Procedure 2005-66), some tribal employers, depending on their employer identification number may be "Cycle A" filers, with determination letter applications due by January 31, 2007. Code Section 414(d) plans, on the other hand, are deemed to fall under Cycle C.

Under Notice 2006-89, tribal employers have until September 30, 2007 to split or convert their "commercial" plans from their Code Section 414(d) plans. Thus, there will be no "commercial plan"

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[9] Again, there is no legislative history indicating an intent to disenfranchise tribal court jurisdiction. However, these issues, if not coordinated through deferential regulations from both IRS and DOL could lead to legal challenges based on tribal sovereignty.

[10] If these employees are subject to ERISA, they also may be prevented from establishing a non-qualified plan unless they qualify for "top hat" treatment.

document in existence by the Cycle A submission date, even though the split or converted plan will be effective retroactive to the Cycle A submission period.

Given that the entire determination letter process has been closed to tribal government plans since 2004, we urge extended relief for all tribal submissions and remedial amendment deadlines from the initial 2004 no-rule date until further guidance is issued.

6. Guidance should provide relief to tribal employers who adopt safe harbor plans during the transition period.

Government plans are exempt from ADP and ACP tests. Commercial plans are not. In an abundance of caution, many tribal employers have elected to adopt safe harbor features prior to the actual splitting of commercial and governmental plans. Current safe harbor guidance requires the safe harbor formula to be in effect for a full plan year and be adopted on a prospective basis. Unfortunately, changes to tribal plans require formal government action and many tribal governments could not adopt these features prior to their PPA effective date.

As these changes are proactive in nature and benefit the non-highly paid group, we would urge relief from the prospective adoption and the advance notice requirements.

7. Guidance should confirm that plans that are under VCP review for years prior to the PPA effective date are entitled to rely on Code Section 414(d) status.

Prior to the PPA, there was no guidance from the IRS or DOL indicating that tribal governments were not entitled to "government" status under Code Section 414(d). To the contrary, many tribes across the county (including gaming enterprises) routinely received determination letters approving their plans under the government sector rules. Several tribes also requested express guidance from the IRS and DOL on these matters, in a good faith effort to comply with the law, but no guidance was published.

In fact, since 2004, there has been a "no-rule" position foreclosing tribes' ability to seek guidance on these very issues. Enactment of the PPA this past August, therefore, was the first indication that any tribal entities are excluded from government status under these rules. Given that the PPA has an express "prospective" effective date, we urge guidance that will confirm that "commercial" rules will not be applied retroactively. While the Commissioner has already confirmed this in two separate letters, we are aware of several tribes who have "VCP:" applications being held because the agents working those files are not sure whether they can apply the Code Section 414(d) rules prior to the PPA's effective date.

8. The Guidance should provide additional time for tribal governments to make those changes necessary for compliance with the new rules.

Notice 2006-89 currently provides tribal employers through September 30, 2007 within which to adopt documents necessary to split or convert their "commercial" and "government" plans. We would urge an extended period to adopt documents until after further guidance is issued, and to extend operational good faith compliance in the interim period.

In addition to splitting the plans into commercial and government programs, and determining the threshold issue of who will be "commercial", many testing and compliance provisions appearing in those new documents will need to reflect the technical issues outlined above. Standard prototype plan documents available to tribal employers at this time will not reflect any of the foregoing. Thus, most tribal employers will need to adopted individual design plan documents. Those who adopt prototypes because of fast approaching deadlines may find themselves vulnerable to improper products and documents based on incorrect assumptions.

A decade ago, tribal employers across the country were improperly sold 403(b) tax sheltered annuity programs largely because there was a lack of guidance regarding what tribal employers could or could not do. While it took Congressional action to remedy that situation through the Small Business Job Protection Act, tribes still face 403(b) program compliance issues that have not been resolved.

Given the severity of the actions required for tribes to comply with these changes, we hope that the Service will grant an extended transition period to ensure that the changes that are ultimately made will be done in a prudent fashion.

9. Additional time for comment and consultation with tribes on a government-to-government basis under Executive Order 13175 is needed before proposed regulations are published.

During the extended transition period, we urge the Service to engage in consultation pursuant to Executive Order 13175. This comment letter is not a substitute for the individual experiences and impact that tribes across the country will feel as a result of the PPA changes.

Organizations such as the Profit Sharing / 401(k) Council of America (PSCA), the Native American Finance Officers Association (NAFOA), and the National Congress of American Indians (NCAI), while not a substitute for individual consultation, can also be utilized in a cooperative manner to enlist additional comment on a broader or regional scale.

Conclusion:

We appreciate the opportunity to provide comments, and the effort being made to solicit tribal input. Given the economic and sovereignty impact that guidance under the PPA may have, however, we would urge the IRS to extend the period for comment and consultation pursuant to Executive Order 13175 before regulations are proposed.

With regard to determining the ultimate question as to whether an employee is performing an "essential" government function or a "commercial" activity, we urge the Service to defer to the elected governing councils themselves. An elected sovereign, guided by factors set forth in broad based guidance, is in the best position to make these determinations.

The PPA issues by their very nature are complex. Some issues are also clearly better communicated in person than through written comment. We would encourage you to contact the undersigned for further discussion as you work through these important matters.

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