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STRAUSS HAUER & FELD LLP

March 12, 2009

AMERICAN INDIAN LAW AND POLICY ALERT

INDIAN FINANCE PROVISIONS INCLUDED IN THE AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009

The American Recovery and Reinvestment Act of 2009 ("Recovery Act") includes a provision that expands a tribal government's ability to issue tax-exempt bonds and creates a new tax credit bond program relative to the construction of Indian schools. It also includes other provisions relevant to tribes—Build America bonds, clean renewable energy bonds and qualified energy conservation bonds.

TRIBAL ECONOMIC DEVELOPMENT BONDS (SECTION 1402)

Like state governments, tribal governments are responsible for providing a host of services not only for their members but also for non-members who live on or near tribal lands. These services include fire, police and ambulance service, road and bridge maintenance and a broad range of other services. Unlike state governments, however, tribal governments faced severe restrictions on their ability to finance development through debt instruments. Up until now, the tax law, Internal Revenue Code Section 7871(c), prevented tribes from issuing tax-exempt bonds for any project unless the project met the so-called "essential governmental function" test. That is, in order for interest on a tribal bond to be exempt from federal tax, the bond must be issued for activities that are "governmental" in nature, which did not "include any function which is not customarily performed by State and local governments with general taxing powers." The test has been very narrowly construed by the Internal Revenue Service (IRS). No similar requirement applies to state and local governments when they issue tax-exempt debt.

The Recovery Act authorizes tribal governments to issue $2 billion of tax-exempt bonds for projects that were not previously authorized. Importantly, these projects do not have to be used in the exercise of an "essential governmental function." No proceeds of the bonds, however, may be used for class II or class III gaming facilities or for any facility located outside of an Indian reservation.

A system for allocating these bonds has yet to be put in place.

BUILD AMERICA BONDS (SECTION 54AA)

State and local governments generally receive federal financial support through the federal tax exemption for interest on municipal bonds. The Build America bonds provision, added as

Internal Revenue Code Section 54AA by the Recovery Act, subsidizes certain state and local government projects otherwise eligible for tax-exempt financing in a different way. The issuer may irrevocably elect to have an otherwise tax-exempt bond treated as a "taxable governmental bond." The holder of such a bond will accrue a federal tax credit (against both regular and alternative minimum tax) in the amount of 35 percent of the interest paid on the interest payment dates. Both the interest paid and the credit must be included in gross income as interest income by the holder. Because the credit is also included in income, the Joint Committee on Taxation anticipates that state and local issuers will issue bonds paying interest at rates approximately equal to 74.1 percent of a comparable taxable bond's interest rate.

This provision applies to bonds issued after the date of enactment and before January 1, 2011. The program is estimated to cost $4.348 billion over 10 years.

At a public forum, a representative for the IRS indicated the IRS's initial read is that a tribe should be considered a "local government" under this section.

QUALIFIED SCHOOL CONSTRUCTION BOND (SECTION 1521)

The federal government is responsible for 184 Indian schools funded by the Bureau of Indian Affairs (BIA). The BIA funds approximately 4,500 facilities in Indian country, which serve more than 60,000 students and more than 238 federally recognized Indian tribes located in 23 states. As of 2000, half of the school facilities in the BIA's inventory exceeded their useful lives of 30 years, and more than 20 percent were over 50 years old. Direct appropriations do not keep up with the need to repair and replace these facilities.

The Recovery Act creates a new category of tax credit bonds—qualified school construction bonds. These bonds must meet three requirements: (1) 100 percent of the bond's available project proceeds must be used to construct, rehabilitate or repair a public school facility or to acquire land on which such a bond-financed facility is to be constructed; (2) the bond must be issued by the state, local or tribal government within which such school is located; and (3) the issuer must designate the bond as a qualified school construction bond. The Recovery Act provides $400 million to tribal governments for these bonds. The initial allocation for 2009 will be $200 million and the remainder will be allocated in 2010.

Additional authorizing language may be necessary to ensure that all tribes have access to the school construction bonding authority. As with the tax-exempt bonding authority, a system for allocating these bonds has yet to be put in place.

OTHER TAX PROVISIONS

The Recovery Act also raises the national limitation for clean renewable energy bonds (CREBs) to as much as $1.6 billion. In addition, the Recovery Act authorizes the allocation of $2.4 billion in qualified energy conservation bonds.

CONTACT INFORMATION

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