Gavin Clarkson

Energy to Empower New Mexico

September 22, 2019

The Honorable Jay Clayton, Chairman
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

RE: Accredited Investor - Tribal Governments - 84 FR 30460, Document Number 2019-13255

Dear Chairman Clayton:

As the first tribal member to ever earn a doctorate from the Harvard Business School and the nation's leading scholar in tribal finance as recognized by the Financial Times, I am writing to express my support for a regulatory fix that would define tribal governments as accredited investors under Regulation D (17 C.F.R. §§ 230.501-230.508) of the Securities Act of 1933.

As defined under the Act, an accredited investor is a state plan, person, or institution that the SEC deems capable of taking on the economic risk of investment in unregistered securities. Limiting the ability of unaccredited investors to participate in unregistered securities is seen as adding a protective layer between investment securities and the general public. As I have written previously, and as noted by the Native American Finance Officers Association ("NAFOA") in their comments, the authors of neither the Act nor the regulation apparently considered tribal governments as potential investors. Correcting this oversight is important for both the continued growth and diversification of tribal economies and the management of tribal government economic risk.

My colleagues and I at Native American Capital started working on this issue in 2005 and submitted a position paper to the SEC in 2006.[1] We also began discussions with the SEC on the issue and alerted the National Congress of American Indians ("NCAI") to the need for a change. NCAI then commissioned a "Red Paper,"[2] based in part on our original position paper, for presentation at the National Native American Economic Summit in Phoenix, Arizona in May 2007. I later expanded upon that paper and published an article in the Colorado Law Review entitled *Accredited Indians: Increasing the Flow of Private Equity into Indian Country as a Domestic Emerging Market*.[3]

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[1] Clarkson,G., Falkson, J., Rubin, M., Hillabrant, W., NATIVE AMERICAN TRIBES REQUIRE REG D CHANGE (2006), available at http://www.sec.gov/rules/other/265-23/nac020306.pdf

[2] Clarkson,G., CAPITAL AND FINANCE ISSUES: TRIBAL ENTERPRISES (2007), available at https://web.archive.org/web/20071009102112/http://www.ncai.org/ncai/econpolicy/CapitalandFinancePapers.pdf

[3] Clarkson, G., ACCREDITED INDIANS: INCREASING THE FLOW OF PRIVATE EQUITY INTO INDIAN COUNTRY AS A DOMESTIC EMERGING MARKET (March 1, 2008). University of Colorado Law Review, Vol. 80, No. 285, 2009; U of Michigan Law & Economics, Olin Working Paper No. 08-002. Available at SSRN: https://ssrn.com/abstract=1107907 or http://dx.doi.org/10.2139/ssrn.1107907

That article presented Indian Country as America's domestic emerging market, and as with other of emerging markets, many successful businesses in Indian Country are starving for expansion capital. The US Department of the Treasury estimates that the private equity deficit in Indian Country is $44 billion. While the handful of wealthier tribes might be logical investors in private equity funds deploying capital in Indian Country, the existing securities laws present a significant impediment, including Regulation D's failure to treat tribes as "accredited investors," thus denying those tribes the ability to participate in the private equity market. Since there is no principled reason to exclude tribes from the list of accredited investors, I argued for extending accredited investor status to tribes.

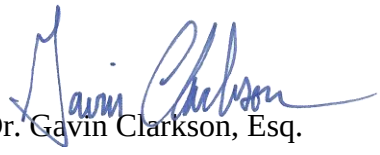
The article is attached as an appendix to my comments, in part to provide empirical support for the recommended changes to Regulation D, but also to highlight the fact that a proposed rule change was already underway in 2007 which would have solved this issue. As I noted in my article, the comment period closed on October 9, 2007, with no opposition to the inclusion of tribes as accredited investors. Unfortunately, the Great Recession and the anemic pace of the subsequent recovery diverted attention away from these needed changes to Regulation D.

I therefore join with NAFOA in requesting that the SEC amend the eligible entities excluded under Regulation D (17 C.F.R. §§ 230.501 (a)(1) of the Securities Act to include "any investment established and maintained by a tribal government, its political subdivisions, or any agency or instrumentality of a tribal government or its political subdivisions, for the benefit of its citizens (members), if such investment has total assets in excess of $5,000,000 in non-trust assets." Additionally, the term "non-trust asset" should be defined as "an asset that is under the direct control of a tribe or tribal entity, and which is not held in trust by the United States for the benefit of the tribe" to provide clarity. Also, the term "political subdivision" should be defined as to include a tribal corporation formed under Section 17 of the Indian Reorganization Act or the comparable provision of the Oklahoma Indian Welfare Act.

I respectfully request the SEC give full consideration to NAFOA's request to include tribal governments as accredited investors, and I incorporate the balance of their comments herein by reference.

Please feel free to contact me by phone at [redacted]) or by email at [redacted] if you have questions, concerns, or need further information.

Sincerely,



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ACCREDITED INDIANS: INCREASING THE FLOW OF PRIVATE EQUITY INTO INDIAN COUNTRY AS A DOMESTIC EMERGING MARKET

GAVIN CLARKSON*

Indian Country is America's domestic emerging market, and, as in other emerging markets, many successful businesses in Indian Country are starving for expansion capital. The U.S. Treasury estimates that the private-equity deficit in Indian Country is $44 billion. While the handful of wealthier tribes might be logical investors in private-equity funds deploying capital in Indian Country, the existing securities laws present a significant impediment. In particular, Regulation D of the Securities Act of 1933 does not treat tribes as "accredited investors," thus denying those tribes the ability to participate in the private-equity market. Since there is no principled reason to exclude tribes from the list of accredited investors, this Article makes the case for extending accredited investor status to tribes.

INTRODUCTION

While discussions of emerging markets usually focus on economic development in third world countries, most Indian tribes have an economy on par with those same countries. Ex-

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tensive land bases, spread-out communities, and homesteads mired in one long-standing poverty cycle characterize most reservations.[1] Just as with other emerging markets, the need for economic development in Indian Country[2] remains acute and affects nearly every aspect of reservation life.

Contrary to popular belief, gaming does not provide a significant economic stimulus for most tribal economies. Most of the more than 560 federally-recognized Indian tribes[3] do not have any form of gaming operations,[4] and of those that do, only a small handful generate significant revenues.[5] While a small number of tribes near major metropolitan centers operate successful gaming enterprises, hundreds of tribes have not entered the gaming industry, and many that have participated operate casinos located far from population centers.[6] Thus, the economic benefits of gaming are not universally distributed

1. *Entrepreneurial Sector Is the Key to Indian Country Development*, INDIAN COUNTRY TODAY, Sept. 11, 2002, at A2.

2. 18 U.S.C. § 1151 (2006) defines "Indian Country" as:

> (a) all land within the limits of any Indian reservation under the jurisdiction of the United States Government, notwithstanding the issuance of any patent, and, including rights-of-way running through the reservation,
>
> (b) all dependent Indian communities within the borders of the United States whether within the original or subsequently acquired territory thereof, and whether within or without the limits of a state, and
>
> (c) all Indian allotments, the Indian titles to which have not been extinguished, including rights-of-way running through the same.

3. Indian Entities Recognized and Eligible to Receive Services from the United States Bureau of Indian Affairs, 70 Fed. Reg. 71,194 (Nov. 25, 2005).

4. According to the National Indian Gaming Association, only 224 tribes have gaming operations of any kind as of 2005. NAT'L INDIAN GAMING ASS'N, AN ANALYSIS OF THE ECONOMIC IMPACT OF INDIAN GAMING IN 2005, at 2 (2005), *available at* http://www.indiangaming.org/NIGA_econ_impact_2005.pdf.

5. *See* NAT'L GAMBLING IMPACT STUDY COMM'N, NATIONAL GAMBLING IMPACT STUDY COMMISSION REPORT 2-10 (1999), *available at* http://govinfo.library.unt.edu/ngisc/reports/2.pdf ("The 20 largest Indian gambling facilities account for 50.5 percent of total revenues, with the next 85 accounting for [only] 41.2 percent. Additionally, not all gambling facilities are successful. Some tribes operate their casinos at a loss and a few have even been forced to close money-losing facilities."). Note also that many tribes that do generate significant revenues often must share those revenues with the state as part of the compacting process of the Indian Gaming Regulatory Act. *See* 25 U.S.C. §§ 2701–2721 (2006). In some cases, such as with the Mohegan and Mashantucket Pequot tribes in Connecticut, the revenue share is as high as twenty-five percent. *See, e.g.*, Gavin Clarkson & Jim Sebenius, Leveraging Tribal Sovereignty for Economic Opportunity: A Strategic Negotiations Perspective 63 (presented at *Native Issues Research Symposium*, Harvard University Native American Program, Dec. 2003) (on file with author).

6. *See* Donald L. Barlett & James B. Steele, *Wheel of Misfortune*, TIME, Dec. 16, 2002, at 44.

throughout Indian Country. For example, the unemployment rate still hovers around fifty percent for Indians who live on reservations, nearly ten times that for the nation as a whole. More than one third of American Indian children live in poverty.[7]

Because small business drives much of the U.S. economy, an increase in small-business activity is a rational step towards improving employment levels and other aspects of reservation economies. Even when Indian Country businesses succeed initially, however, lack of access to expansion capital, particularly equity capital, severely constrains their ability to grow and create jobs. The following two examples illustrate the problem.

Native American Natural Foods of Kyle, South Dakota, started small but grew exponentially before running into significant capacity constraints. Its primary product, the Tanka Bar, is a bison meat and cranberry energy bar based on the traditional Lakota recipe for *wasna*.[8] Tanka bars are so popular that stores across the country cannot keep them on the shelves.[9] Demand for the Tanka Bar increased so rapidly that the company's founders, Mark Tilsen and Karlene Hunter, quickly ran into production capacity constraints. The day I visited the headquarters of Native American Natural Foods in June of 2008 was the same day that Regis Philbin ate a Tanka Bar on live television.[10] Within hours, the company sold nearly an entire month's worth of production.

The philosophy behind the Tanka Bar is multifaceted. Its creators aim for economic development for the Lakota Pine Ridge Reservation, restoration of traditional diet to Native American lives, assistance to bison ranchers looking for meat markets, and a brand name to become a household name, opening the way for Native American Natural Foods' future endeavors.[11] While numerous opportunities exist for national

7. *See, e.g.*, NAT'L CTR. FOR EDUC. STATISTICS, U.S. DEP'T OF EDUC., AMERICAN INDIAN AND ALASKA NATIVE CHILDREN: FINDINGS FROM THE BASE YEAR OF THE EARLY CHILDHOOD LONGITUDINAL STUDY, BIRTH COHORT (ECLS-B) 3 (2005), *available at* http://nces.ed.gov/pubs2005/2005116.pdf.

8. *See generally* Tanka Bar, http://www.tankabar.com (last visited Nov. 16, 2008).

9. Dan Daly, *Tanka Bar Maker Scrambles to Meet Soaring Demand*, RAPID CITY J., Jan. 19, 2008, http://www.rapidcityjournal.com/articles/2008/01/19/news/top/doc47903fee8b270243114583.txt.

10. Heidi Bell Gease, *Tanka Bar on Regis & Kelly*, RAPID CITY J., June 12, 2008, http://www.rapidcityjournal.com/articles/2008/06/12/news/local/doc4850a1f4c75fe933045587.txt.

11. Daly, *supra* note 9.

distribution, the Tanka Bar operation lacks adequate production capacity and cannot produce enough bars to meet existing demand.[12]

Another initially successful Indian Country business that desperately needs an equity infusion in order to expand is Sister Sky, a bath and body products business created by sisters Monica Simeon and Marina TurningRobe.[13] The company sells bath and body products to hotels at tribal gaming resorts and operates an online products site.[14] Founded in 1998, Sister Sky's revenue in 2007 was over $550,000, up from $225,000 in 2006.[15] Given its initial success, Sister Sky would like to expand into retail with specialty shops in casino resorts.[16]

Manufacturing and logistics, however, are two of Sister Sky's greatest challenges.[17] The company quickly outgrew its $100,000 production line on the Spokane Reservation in Washington State, and although it might be able to self-finance a new headquarters in about five years, current capacity constraints severely hinder its ability to grow and create new jobs.[18]

Sister Sky and Native American Natural Foods are just two examples of solid, well-run Indian Country businesses that are starving for private equity to meet their expansion needs. A logical source for the capital necessary to increase small business activity in Indian Country would seem to be the small number of tribes that have reaped significant profits from Indian gaming. Many of those wealthier tribes feel an obligation to invest back into the poorer areas of Indian Country. Historically, the only mechanism for deploying this capital has been through direct investment. Many tribal councils, however, have neither the necessary experience to appropriately evaluate such investments nor the time to thoroughly examine numerous direct investment opportunities. Furthermore, direct investment by only a handful of wealthy tribes would not solve the overall private-equity gap in Indian Country.

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12. *See id*.

13. Patricia Gray, *Sister Act*, FORTUNE SMALL BUS., Dec./Jan. 2008, at 33, 33–36, *available at* http://money.cnn.com/2007/12/03/smbusiness/Sister_sky.fsb/index.htm.

14. *Id*.

15. *Id*.

16. *Id*.

17. *Id*.

18. *Id*.

The logical alternative is for tribes to deploy equity capital in the same way as other wealthy individuals or corporations: investing in a private-equity or venture-capital fund where financial professionals can evaluate various businesses and select the best opportunities in order to maximize investment returns. Such funds, which include venture-capital funds, provide financing for early- and late-stage private companies. These funds raise their capital from "third-party investors seeking high returns based on both the risk profiles of the companies and the near-term illiquidity of these investments."[19] Unfortunately, wealthy tribes have not been able to participate in private-equity investing because, under Regulation D ("Reg D") of the Securities Act of 1933,[20] Indian tribes are not included in the list of "accredited investors."[21]

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19. Roger Leeds & Julie Sunderland, *Private Equity Investing in Emerging Markets*, J. APPLIED CORP. FIN., Fall 2003, at 111, 111.

20. Pub. L. No. 73-22, 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a–77aa).

21. Rule 501(a) of Regulation D of the Securities Act of 1933 states that an

> *Accredited Investor* shall mean any person who comes within any of the following categories, or who the issuer reasonably believes comes within any of the following categories, at the time of the sale of the securities to that person:
>
> a. Any bank as defined in section 3(a)(2) of the Act, or any savings and loan association or other institution as defined in section 3(a)(5)(A) of the Act whether acting in its individual or fiduciary capacity; any broker or dealer registered pursuant to section 15 of the Securities Exchange Act of 1934; any insurance company as defined in section 2(a)(13) of the Act; any investment company registered under the Investment Company Act of 1940 or a business development company as defined in section 2(a)(48) of that Act; any Small Business Investment Company licensed by the U.S. Small Business Administration under section 301(c) or (d) of the Small Business Investment Act of 1958; any plan established and maintained by a state, its political subdivisions, or any agency or instrumentality of a state or its political subdivisions, for the benefit of its employees, if such plan has total assets in excess of $5,000,000; any employee benefit plan within the meaning of the Employee Retirement Income Security Act of 1974 if the investment decision is made by a plan fiduciary, as defined in section 3(21) of such act, which is either a bank, savings and loan association, insurance company, or registered investment adviser, or if the employee benefit plan has total assets in excess of $5,000,000 or, if a self-directed plan, with investment decisions made solely by persons that are accredited investors;
>
> b. Any private business development company as defined in section 202(a)(22) of the Investment Advisers Act of 1940;
>
> c. Any organization described in section 501(c)(3) of the Internal Revenue Code, corporation, Massachusetts or similar business trust, or partnership, not formed for the specific purpose of acquiring the securities offered, with total assets in excess of $5,000,000;

Reg D specifies rules governing the sale of securities by private companies and exemptions from federal and state securities registration requirements. Small Business Investment Companies ("SBICs") and other small private-equity firms regularly avail themselves of the so-called "Reg D exemption." While there are a number of pathways through which a private-equity firm can avail itself of this filing exemption, as a practical business matter, the pathway most successfully followed is to offer securities only to accredited investors.

Rule 501(a) of Reg D defines who is or is not an "accredited investor" within the meaning of the Reg D exemption. Private-equity funds strongly prefer to sell securities to accredited investors to assure that the companies completely comply with Federal and State securities laws.[22] While Reg D permits a private company to sell its securities to categories of investors other than accredited ones, these alternative scenarios create significant legal complexities and business risks that increase the costs of raising capital (for example, risk premiums paid to investors, as well as much higher legal fees, and the increased costs associated with the preparation of more detailed disclosure documents).[23]

Generally, securities lawyers advise startup private-equity funds to restrict the sale of securities (that is, raise their "blind pool" of capital) to accredited investors, given the high-risk na-

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d. Any director, executive officer, or general partner of the issuer of the securities being offered or sold, or any director, executive officer, or general partner of a general partner of that issuer;

e. Any natural person whose individual net worth, or joint net worth with that person's spouse, at the time of his purchase exceeds $1,000,000;

f. Any natural person who had an individual income in excess of $200,000 in each of the two most recent years or joint income with that person's spouse in excess of $300,000 in each of those years and has a reasonable expectation of reaching the same income level in the current year;

g. Any trust, with total assets in excess of $5,000,000, not formed for the specific purpose of acquiring the securities offered, whose purchase is directed by a sophisticated person as described in Rule 506(b)(2)(ii);

h. Any entity in which all of the equity owners are accredited investors.

GAVIN CLARKSON, JOE FALKSON, MARCO RUBIN & WALTER HILLABRANT, NATIVE AMERICAN CAPITAL, LP, POLICY BRIEFING: NATIVE AMERICAN TRIBES REQUIRE REG D CHANGE 2–3 (2006), *available at* http://www.sec.gov/rules/other/265-23/nac020306.pdf (quoting 17 C.F.R. § 230.501 (2008)).

22. *Id.* at 1.

23. *Id.*

ture of equity investments.[24] The result of such a restriction is that any private investment firm raising its capital from non-accredited investors will pay higher costs for these funds.[25]

While some of the current federal regulations and policies that harm tribal economies are a result of overt hostility towards tribes,[26] this Article suggests that the exclusion of tribes from the category of accredited investors results from mere oversight, or "benign neglect." Nevertheless, the impact of this benign neglect has been devastating. According to the U.S. Treasury Department, the equity investment gap in Indian Country is $44 billion, and private enterprise in Indian Country needs that capital.[27] As described above, however, federal regulations and policies effectively bar the tribes that would be the primary candidates to help remedy this situation.

It is also logical to assume that the lack of tribal investment in Indian Country's emerging economy creates some degree of hesitation among non-Indian investors. As such, private enterprise in Indian Country is unable to get past the tipping point created by the exclusion of tribal investment capital and the concomitant reluctance of non-Indian investment capital.

I encountered this tipping point first-hand in 2005 when I joined the board of Native American Capital, the first ever native-owned, Indian-Country-focused, private-equity fund. The tribes wanted to follow Wall Street's lead as they began to explore private equity. Cognizant of the handful of wealthy tribes, Wall Street repeatedly asked, "Where is the tribal investment?" Even after the wealthier tribes began to consider making the first move into private equity, they ran into the Reg D hurdle, and Wall Street continued to ask "where are the tribes?"

The end result was a typical "catch 22." Wealthier tribes were prevented from investing in private-equity funds, even if those funds had an Indian Country focus, and poorer tribes were unable to tap into private equity, in part, because Wall

24. *Id.* at 2.

25. *Id.*

26. *See* Gavin Clarkson, *Tribal Bonds: Statutory Shackles and Regulatory Restraints on Tribal Economic Development*, 85 N.C. L. REV. 1009, 1065 (2007) [hereinafter Clarkson, *Tribal Bonds*].

27. CMTY. DEV. FIN. INSTS. FUND, U.S. DEP'T OF TREASURY, THE REPORT OF THE NATIVE AMERICAN LENDING STUDY 2 (2001), *available at* http://www.cdfifund.gov/docs/2001_nacta_lending_study.pdf [hereinafter CDFI].

Street looks to the wealthier tribes as the logical first movers for Indian Country investment.[28]

Surprisingly, the regulatory change that could potentially push Indian Country past this private-equity tipping point was simple and straightforward: amend Rule 501 of Reg D to include federally recognized Indian Tribes and their instrumentalities as accredited investors. The challenge, however, was to get such a proposed rule change on the Security and Exchange Commission's ("SEC") agenda. My colleagues and I at Native American Capital developed and submitted a position paper to the SEC in 2006.[29] We also began discussions with the SEC on the issue[30] and alerted the National Congress of American Indians ("NCAI") to the need for a change. NCAI then asked me to draft a "Red Paper,"[31] based in part on our original position paper, for presentation at the National Native American Economic Summit ("Summit") in Phoenix, Arizona in May 2007. This Article is the final written evolution of those prior efforts on the Reg D issue.

The intention of the Summit was to set the Bush Administration's Indian Country agenda for its final two years. Not surprisingly, proposals that were revenue neutral or, better yet, revenue enhancing, were of particular interest. Augmenting the position paper with an economic model showing that amending Rule 501 would actually be revenue enhancing, our proposal made it to the short list of recommendations.[32]

In part because we had already laid the groundwork, the SEC quickly responded to the Summit recommendation by incorporating our proposal into a larger set of amendments to Reg D.[33] The comment period closed on October 9, 2007, with no opposition to the inclusion of tribes as accredited investors.

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28. There are of course other impediments to equity capital access for Indian Country businesses. *See, e.g.*, *infra* Part III.C.

29. CLARKSON, FALKSON, RUBIN & HILLABRANT, *supra* note 20.

30. *See* E-mail exchange between Gavin Clarkson, Joe Falkson & Gerald J. Laporte, Chief, Office of Small Business Policy, Securities and Exchange Commission (Dec. 3, 2005) (on file with author).

31. As opposed to a "White Paper." *See* GAVIN CLARKSON, CAPITAL AND FINANCE ISSUES: TRIBAL ENTERPRISES (2007), *available at* http://www.ncai.org/ncai/econpolicy/CapitalandFinancePapers.pdf.

32. DEP'T OF INTERIOR & NAT'L CONG. OF AM. INDIANS, NATIVE AMERICAN ECONOMIC POLICY REPORT 14 (2007), *available at* http://www.ncai.org/ncai/econpolicy/Summit_Policy_Report_Fnl2007NS.pdf.

33. Revisions of Limited Offering Exemptions in Regulation D, 72 Fed. Reg. 45,116 (Aug. 10, 2007).

While legal scholars always hope that their work will influence policy and make a difference in the world, this Article is unique in that it substantially contributed to a significant policy change while still in working paper form. This expanded version recounts the substance of the policy and economic arguments that my colleagues and I made, while also providing some additional background and context.

Part I of this Article makes the argument for viewing Indian Country as an emerging market, detailing the challenges that both tribes and tribal members face when seeking to access the capital market, either for debt or for equity. For those readers unfamiliar with federal Indian law and policy, Part II of this Article discusses the nature of Indian tribes and their relationship to the federal government, highlighting the origins of federal Indian policy. Part III focuses on economic development as one particular aspect of that policy and examines the process of business formation in Indian Country, including the role of Community Development Financial Institutions ("CDFIs") in the initial startup phase of entrepreneurial development. Part III also examines private equity's potential role in providing expansion capital for Indian Country businesses. This Part concludes by detailing the interplay between private equity and the securities laws, focusing also on the history of the accredited investor standard. Part IV presents the various policy and economic rationales for treating tribes as accredited investors that ultimately succeeded in bringing about the desired policy change. The Article concludes with a brief exploration of related topics for future research.

I. INDIAN COUNTRY AS AN EMERGING MARKET

The socio-economic challenges that often burden tribal communities include low educational achievement,[34] high poverty,[35] and low per capita income.[36] As mentioned earlier, the

34. RAYMOND C. ETCITTY, ADVISORY COMM. ON TAX EXEMPT & GOV'T ENTITIES, TRIBAL ADVICE AND GUIDANCE POLICY II-7 (2004), *available at* http://ftp.qai.irs.gov/pub/irs-tege/act_rpt3_part2.pdf.

35. The average percentage of American Indians living in poverty is 25.9%, compared to 11.9% for the general population. *See* U.S. DEP'T OF COMMERCE, POVERTY IN THE UNITED STATES: 2000, at 7 (2001), *available at* http://www.census.gov/prod/2001pubs/p60-214.pdf.

36. Per capita income for American Indians in 1999 was $12,893, compared to the overall U.S. average of $21,587. *See* U.S. Census Bureau 2000, Fact Sheet, http://factfinder.census.gov (click "Fact Sheet" and select "2000" tab for general

unemployment rate hovers around fifty percent for Indians who live on reservations, nearly ten times that for the nation as a whole, and thirty-four percent of American Indian children live in poverty.[37]

For many tribes, the only sources of capital to address these problems are limited to grants and other assistance from the federal government. Such funds are often insufficient, however, to address the myriad responsibilities facing tribal governments.

Gaming activity does not provide sufficient funds to meet the needs of all tribal governments. As Elsie Meeks, Executive Director of First Nations Oweesta Corporation, stated before the Senate Indian Affairs committee:

> [M]any Americans seem to assume that Indian gaming has 'solved' the problems created by poverty in Native communities. However, . . . gaming has been a boon to only a small number of tribes and many Native people, regardless of income, still lack the basic resources to protect their financial future (even if their governments own profitable enterprises).[38]

All too many tribal governments lack the ability to provide the basic infrastructure most U.S. citizens take for granted, such as passable roadways, affordable housing, and the plumbing, electricity, and telephone services that come with a modern home. According to the U.S. Census Bureau, approximately twenty percent of American Indian households on reservations lack complete plumbing facilities, compared to one percent of all U.S. households.[39] "About 1 in 5 American Indian reservation households dispose[ ] of sewage by means *other than* public sewer, septic tank, or cesspool."[40] The Navajo reservation is the same size as West Virginia, yet it only has 2000 miles of paved roads while West Virginia has 18,000

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population statistics; click "Fact Sheet: Fact Sheet for a Race, Ethnic, or Ancestry Group" and go to "AIAN alone" for American Indian statistics).

37. *See, e.g.*, NAT'L CTR. FOR EDUC. STATISTICS, U.S. DEP'T OF EDUC., *supra* note 7, at 3.

38. *Oversight Hearing on Economic Development: Hearing Before the S. Comm. on Indian Affairs,* 109th Cong. 3 (2006) (statement of Elsie M. Meeks, Executive Director, First Nations Oweesta Corporation), *available at* http://www.oweesta.org/sites/oweesta.org/files/documents/testimony.pdf.

39. BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, STATISTICAL BRIEF: HOUSING OF AMERICAN INDIANS ON RESERVATIONS—PLUMBING 3 (1995), *available at* http://www.census.gov/apsd/www/statbrief/sb95_9.pdf.

40. *Id.*

miles.[41] Investors and employers, even in the most distressed inner cities of the United States, take roads, telephones, electricity, and the like for granted. The absence of such basic infrastructure from large portions of Indian Country poses a daunting barrier to tribal leaders' attempts to attract new private-sector investment and jobs.

Such realities highlight the importance of stimulating economic development to create economic opportunity for tribal members. Many scholars, investors, and tribal officials charged with developing Indian Country economies are well aware that access to capital for tribes and individual Indian entrepreneurs is a significant and pressing problem. The unanswered question is one of capital formation: How do Indian Country businesses obtain the necessary capital? The best solution would be to access the capital markets in the same way that non-Indian businesses do, by financing their own economic activities. As this Article will demonstrate, however, severe impediments to a level playing field continue to plague Indian Country.

Although the primary focus of this Article is increasing the flow of equity financing into Indian Country, an examination of the challenges associated with debt financing is certainly relevant. The next two Sections examine those challenges. Section A considers the challenges faced by tribes that wish to issue bonds, and Section B reviews the problems encountered by individual tribal members who attempt to access bank debt. Sections C and D then examine more fully the challenges associated with equity capital in Indian Country and the concomitant impact of the $44 billion private-equity gap.

A. Tribal Bond Challenges

If tribal governments were to issue economic development bonds, such bonds would benefit businesses on their reservations both directly and indirectly. In an earlier article, *Tribal Bonds*,[42] I pointed out, however, that the Tax Code facially discriminates against tribes and makes such bonding impossible. In addition to highlighting the inability of tribes to issue economic development bonds, *Tribal Bonds* pointed out that more than $50 billion of infrastructure needs go unmet each year in

41. Michael J. Kurman, *Indian Investment and Employment Tax Incentives*, 41 FED. B. NEWS & J. 578, 583 (1994).

42. Clarkson, *Tribal Bonds*, *supra* note 26, at 1009.

Indian Country.[43] These needs occur in such vital sectors as transportation, community facilities, housing, and enterprise development due, in part, to the restrictions imposed on tribal access to the capital markets, specifically the inability of tribal governments to issue tax-exempt debt on the same basis as other governments. Section 7871 of the Internal Revenue Code restricts tribal tax-free bond proceeds to "essential governmental functions," a restriction not applicable to state and municipal bonds.[44] Section 7871(e) "further limits the scope of available tax-exempt bonding to activities 'customarily performed by State and local governments with general taxing powers' without providing any guidance as to when a particular activity becomes 'customary' for a non-tribal government."[45]

Tribal Bonds also detailed how these restrictions have severely limited tribal ability to access the capital markets. Although American Indians make up more than 1.5 percent of the population, tribes issued less than 0.1 percent of the tax-exempt bonds between 2002 and 2004. These restrictions harm the poorer tribes the most, as the difference between tax-exempt and taxable interest rates often determines the feasibility of a project. Without access to tax-exempt rates, poorer tribes simply cannot afford the debt service required to address glaring economic and infrastructure deficiencies.

Tribal governments are also victims of a disproportionate number of enforcement actions by the Internal Revenue Service ("IRS").[46] The IRS audits less than one percent of the tax-exempt municipal offerings each year, but it audits direct tribal tax-exempt issuances within four years of issue thirty times more frequently than tax-exempt issuances of cities and states.[47] In addition, the IRS challenged one hundred percent of tribal conduit issuances.[48] The ambiguity of the statute has led to a number of IRS enforcement actions that simply would not have happened had the issuer not been a tribe. In each of these cases, the activities were substantially similar to activities previously financed by state and local governments without any challenge from the IRS. Based on my research, I have argued that tribal governments should have the same tax-

43. *Id.*
44. *Id.*
45. *Id.* (quoting 26 U.S.C. § 7871(e) (2000)).
46. *See* Clarkson, *Tribal Bonds*, *supra* note 26, at 1046.
47. *Id.* at 1017–18.
48. *Id.* at 1018, 1053.

exempt bonding authority as their state and local counterparts and that expansion of tribal bonding authority would increase federal revenues. Fortunately, as with this Article, that body of research has had some impact. Following the presentation of the research to the Senate Finance Committee[49] and the subsequent publication of *Tribal Bonds*,[50] the 110th Congress introduced legislation[51] to remedy these restrictions.

B. Tribal Member Debt Financing Challenges

As daunting as the challenges seem for tribal entities to obtain debt financing, those same challenges are even greater for individual tribal members who wish to obtain debt financing for their entrepreneurial ventures. The Native American Lending Study ("Lending Study") conducted by the U.S. Treasury Department found that eighty-six percent of Indian Country communities do not have a single financial institution. Members of fifteen percent of Indian Country communities must travel more than one hundred miles to reach a bank or ATM.[52] Additionally, half of the financial institutions providing service to Indian Country only provide ATMs and personal consumer loans, not business loans.[53]

Many banks are skeptical of doing business in Indian Country because they believe they will not be able to enforce contracts made with tribes and members and will instead lose their money.[54] For example, of the financial institutions that are not tribally affiliated but are accessible to reservations, sixty-six percent do not offer start-up business loans on or near the reservations.[55] Seventy-four percent do not offer business

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49. *Encouraging Economic Self-Determination in Indian Country: Hearing before the Subcomm. on Long-Term Growth and Debt Reduction of the S. Comm. on Finance*, 109th Cong. 1 (2006) (written statement of Dr. Gavin Clarkson, Assistant Professor, University of Michigan School of Information, School of Law and Native American Studies) [hereinafter *Clarkson Testimony*], *available at* http://www.senate.gov/~finance/hearings/testimony/2005test/052306testgc.pdf.

50. *See* Clarkson, *Tribal Bonds, supra* note 26.

51. *See* Tribal Government Tax-Exempt Bond Parity Act of 2007, S. 1850, 110th Cong. (introduced July 23, 2007) (eliminates the "Essential Government Function" test and places tribes on equal footing as state and local governments in terms of tax-exempt bonding authority).

52. CDFI, *supra* note 27, at 14.

53. *Id.*

54. Richard J. Ansson, Jr. & Ladine Oravetz, *Tribal Economic Development: What Challenges Lie Ahead for Tribal Nations as They Continue To Strive for Economic Development*, 11 KAN J. L. & PUB. POL'Y 441, 462 (2001).

55. U.S. DEP'T OF THE TREASURY, CMTY. DEV. FIN. INSTS. FUND, NATIVE

microloans, seventy-one percent do not offer small business loans, and eighty percent do not offer larger business loans.[56]

The lack of adequate financial institutions poses a significant challenge for Indian Country businesses when they seek funding. The Lending Study included a financial survey, and more than sixty percent of survey respondents stated that business loans were either "difficult" (thirty-seven percent) or "impossible" (twenty-four percent) to obtain.[57] The level of difficulty increased for business loans over $100,000, with nearly seventy percent rating such loans as difficult or impossible to obtain.[58] Such difficulty may be due, in part, to the fact that "low levels of home-ownership deny [tribal members] the most common form of collateral to obtain loans for purchases or small-business startups."[59] In fact, as of 1999, there were only 471 home mortgages throughout Indian Country.[60] The Lending Study also found that most tribal members "wishing to start a business, purchase a home, or make another large purchase are often not able to qualify for the loans that they need."[61]

C. Indian Country's Equity Investment Gap

In addition to the Lending Study, the Treasury Department also commissioned a companion study to examine private equity in Indian Country ("Equity Study").[62] The Equity Study estimated that Indian Country has $10 billion in equity capital,[63] which is only 0.03% of U.S. total equity.[64] Given the current economic conditions in Indian Country, which are substantially below average for the United States as a whole, Indian Country faces at least a $10 billion equity investment

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AMERICAN LENDING STUDY (2000), *available at* http://www.tribalfinance.org/Documents/2000_nacta_deloitte_touche_final_sur vey_report.pdf.

56. *Id.*

57. CDFI, *supra* note 27, at 2.

58. *Id.*

59. *Id.* at 31.

60. *Id.*

61. *Id.*

62. COMPLEXITY MGMT., INC. & THE JOHNSON STRATEGY GROUP, U.S. DEP'T OF TREASURY, CDFI FUND NATIVE AMERICAN LENDING STUDY: EQUITY INVESTMENT ROUNDTABLE AND RESEARCH REPORT (2001), *available at* http://www.tribalfinance.org/Documents/2001_nacta_final_report_equity.pdf [hereinafter CDFI EQUITY].

63. *Id.* at 55.

64. *Id.* at 7.

gap.[65] The gap between the current Indian Country equity level and the level that should exist based on Indian Country's size relative to the entire United States is $44 billion.[66]

This huge private-equity gap will not be filled until additional private-equity sources are brought to bear, but most venture capitalists and angel investors are either unaware of or unwilling to travel to examine Indian Country venture opportunities.

The Equity Study also found that angel investors and venture capitalists strongly prefer to invest locally.[67] Approximately thirty percent of venture capital investments are in the same metropolitan area as a venture capitalist's office, with some venture capitalists requiring that funded firms relocate closer to the venture capitalist's office as a condition of funding.[68] The Equity Study also highlighted how Indian Country is at a disadvantage in terms of access to professional networks that are critical to accessing private equity:

> Both business angels and venture capitalists obtain their deal flow through a network of trusted sources, most or all of whom are local. They tend to also be networks of people who move in the same circles. As "Eric Schmidt, CEO of Novell confirms, [it] is a myth that anyone can raise venture capital without the right contacts, 'Yeah, right—anybody can raise capital for an Internet company if they know the same guys that I do.'" Native Americans residing in Indian Country are not usually plugged in to these networks because of distance and operating in different social and business groups. The next best way to approach potential investors is through a deal-structurer or matchmaker who is trusted by both sides. But, again, Indian Country business people may not know these sources either for the same reasons. Investors do make some investments from 'over the transom' or from people previously unknown to them. But

65. *Id.* at 55.

66. *Id.*

67. *Id.* at 31. According to the study, location of the investment

> is important to ninety-four percent of angel investors, with over ninety percent of angels investing within a half day's travel time. Sequoia Capital, a leading venture capitalist, uses the bicycle rule. If they cannot ride their bicycle to the firm under consideration, they will not invest. Generally, their radius is between 30 minutes and a day's travel away.

Id. (citations omitted).

68. *Id.*

> these have to be extraordinary opportunities to catch their eye and account for less than 5% of total venture funding.[69]

The concentration of venture capital is high and is located far away from Indian Country. The Equity Study found that firms in the ten states with the greatest Native American populations often had less than one percent of venture capital available.

Although the third-world economic conditions in most of Indian Country present daunting challenges, the economic opportunities in Indian Country suggest that investment in Indian Country's emerging market could yield significant returns. While private-equity investment is the least-used form of financing in Indian Country, as the next Section demonstrates, Indian Country is one of the more promising domestic emerging markets.

D. The Economic Importance of Indian Country

Indian Country's

> population has grown 50% faster than the U.S. population overall over the last five years and is expected to grow at double the U.S. rate by the year 2035. Native American-owned businesses proliferate at seven times the growth rate of all firms in the U.S. and grow sales at more than double the U.S. rate. Native American-owned business revenues grew up to 55% a year from 1987-1992 and are expected to continue to grow at healthy double digit rates.[70]

Indian Country's buying power may almost double in the next decade.

During the 1990s, virtually all job growth in the United States came from small business.[71] Indian Country's rapid economic expansion contrasts with the much slower annual growth rate of five to ten percent for all U.S. businesses, reinforcing the importance of Native American businesses as an engine of growth.[72] As historical sources of U.S. economic growth become less important, it will be increasingly critical to the growth of the overall U.S. economy to stimulate domestic

69. *Id.* (citation omitted).
70. *Id.* at 6 (citations omitted).
71. *Id.*
72. *Id.*

emerging markets. Indian Country is one of those domestic emerging markets that collectively will serve as new engines of U.S. economic growth.

American Indians' buying power was estimated at $35 billion in 2001.[73] Given that half of all Indians live off-reservation, the Treasury Department estimates that Indian Country's buying power is approximately $17 billion.[74] The same study estimated that revenue from Indian Country businesses and trust assets is approximately $25 billion.[75] An additional $9 billion in revenue comes from the federal government, resulting in $34 billion in total Indian Country revenue.[76]

According to the Treasury Department, bridging the first $10 billion of the equity investment gap would produce an additional $16 billion in gross domestic product ("GDP") for Indian Country, increasing it by seventy-six percent.[77] With sufficient equity investment to close the gap, this GDP increase would occur over fifteen to twenty years.[78]

Additional GDP would provide an estimated $10,000 increase in per capita income. Such an increase would bridge the roughly $9000 per person gap in income between American Indians and the U.S. average, lifting more people in Indian Country out of poverty.[79]

Bridging the equity gap should also create or retain roughly 600,000 jobs over the next fifteen to twenty years. This improvement would more than double the current level of employment in Indian Country and would employ the growing Indian Country workforce over the next fifteen to twenty years at a level comparable to the United States overall.[80]

The Treasury Department estimates that if equity capital investment in Indian Country were increased to a level comparable to the rest of the United States, the GDP benefit would increase fourfold.[81]

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73. *Id.*
74. *Id.*
75. *Id.*
76. *Id.* at 6–7.
77. *Id.* at 8.
78. *Id.*
79. *Id.*
80. *Id.*
81. *Id.*

II. A BRIEF HISTORY OF TRIBAL LAW AND POLICY[82]

The notions that led to the various restrictions on tribal economic development, including tribes' omission from the list of accredited investors, are not new. In fact, they trace back to the origins of the United States itself. In *Cherokee Nation v. Georgia*,[83] the first Supreme Court opinion involving an American Indian tribe,[84] Chief Justice Marshall wrote "the relation of the Indians to the United States is marked by peculiar and cardinal distinctions which exist nowhere else."[85] A half century later, the Supreme Court opined that the "relation of the Indian tribes living within the borders of the United States, both before and since the Revolution, to the people of the United States has always been an anomalous one and of a complex character."[86] Even today, Supreme Court justices find that "[f]ederal Indian policy is, to say the least, schizophrenic. And this confusion continues to infuse federal Indian law and our cases."[87] The concept that so confounds both Congress and the courts is that, on one hand, Indian tribes are separate sovereigns, "domestic dependent nations,"[88] that are ensconced as a "third sovereign"[89] in the federal framework. On the other hand, Congress has plenary authority over Indian tribes.[90]

The acknowledged existence of tribal sovereignty, however, has served to balance the exercise of that plenary authority. While each tribe has its own separate history, the struggle to

82. For a more detailed history of tribal law and policy, see Clarkson, *Tribal Bonds*, *supra* note 26.

83. Cherokee Nation v. Georgia, 30 U.S. 1 (1831).

84. An earlier Supreme Court case, *Johnson v. McIntosh*, 21 U.S. 543 (1823), dealt with the issue of who could acquire title to land from Indian tribes, but no tribe was a party to the case.

85. *Cherokee Nation*, 30 U.S. at 15.

86. United States v. Kagama, 118 U.S. 375, 381 (1886).

87. United States v. Lara, 541 U.S. 193, 219 (2004).

88. *Cherokee Nation*, 30 U.S. at 13.

89. In the words of Justice Sandra Day O'Connor, "Today, in the United States, we have three types of sovereign entities—the Federal government, the States, and the Indian tribes. Each of the three sovereigns . . . plays an important role . . . in this country." Sandra Day O'Connor, *Lessons from the Third Sovereign: Indian Tribal Courts*, 33 TULSA L.J. 1, 1 (1997).

90. *See* COHEN'S HANDBOOK OF AMERICAN INDIAN LAW § 1.03[1] (2005 ed.) [hereinafter COHEN 2005]. I was a contributing author for this most recent edition of the HANDBOOK, providing material on tribal finance, tribal corporations, economic development, and intellectual property. Two earlier editions of the HANDBOOK are also referenced in this Article. Felix Cohen's original HANDBOOK was published in 1941. The HANDBOOK was substantially revised and reissued in 1982.

maintain a separate sovereign existence is common to most tribes. The economic importance of that struggle cannot be overstated, particularly in the modern context, as the "first key to economic development is sovereignty."[91] Thus, it is important to review the origins of the federal Indian law and policy before addressing the modern context.

Despite rhetoric to the contrary,[92] practical realities clearly shaped the early legal relations between the Indians and colonists.[93] The necessity of getting along with powerful and militarily capable Indian tribes dictated that the settlers seek Indian consent to settle if they wished to live in peace and safety, buying lands that the Indians were willing to sell rather than displacing them by other methods.[94] As a result, the English colonial governments purchased most of the lands from the Indians.[95] For all practical purposes, during this period "the Indians were treated as sovereigns possessing full ownership rights to the lands of America."[96]

As the newly formed United States began its inexorable march westward, Indians gave up their lands not by force but by treaty in return for, among other things, the establishment of a trust relationship,[97] often in specific consideration for the

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91. Stephen Cornell, *Sovereignty, Prosperity and Policy in Indian Country Today*, 5 COMMUNITY REINVESTMENT 5, 6 (1997).

92. *See* Clarkson, *supra* note 26, at 1020–1025.

93. *See* COHEN'S HANDBOOK OF AMERICAN INDIAN LAW 5 (1982) [hereinafter COHEN 1982].

94. *Id*. Despite devastating outbreaks of disease, the Indians would continue to outnumber the European settlers for several decades.

95. *Id*. The Dutch similarly opted to obtain land via consented purchase rather than more bellicose methods.

96. *Id*.

97. The scope of the trust relationship is multi-faceted. "Many treaties explicitly provided for protection by the United States." COHEN 1982, *supra* note 93, at 65. *See, e.g.*, Treaty with the Creeks, art. 2, Aug. 7, 1790, 7 Stat. 35, *reprinted in* 2 CHARLES J. KAPPLER, INDIAN AFFAIRS, LAWS AND TREATIES 25 (1904) [hereinafter Treaty with the Creeks]; Treaty with the Kaskaskia, art. 2, Aug. 13, 1803, 7 Stat. 78, *reprinted in* KAPPLER, *supra,* at 67 [hereinafter Treaty with the Kaskaskia].

Other treaties provided the means for subsistence. *See, e.g.*, Fort Laramie Treaty, Sept. 17, 1851, 11 Stat. 749, *reprinted in* FRANCIS PAUL PRUCHA, DOCUMENTS OF UNITED STATES INDIAN POLICY 84 (3d ed. 2000) (providing for subsistence rations for the Sioux.); Treaty with the Western Cherokees art. 8, May 6, 1828, 7 Stat. at 313, *reprinted in* KAPPLER, *supra,* at 290 [hereinafter Treaty with the Western Cherokees]; COHEN 1982, *supra* note 93, at 81 ("[E]ach Head of a Cherokee family . . . who may desire to remove West, shall be given, on enrolling himself for emigration, a good Rifle, a Blanket, and a Kettle, and five pounds of Tobacco: (and to each member of his family one Blanket,) . . . a just compensation for the property he may abandon.").

Indians' cession of their land.[98] It is important to note that the federal government enacted these treaties as a government-to-government relationship between the United States and the tribes, as collective political entities.[99] From the beginning of its political existence, therefore, the United States "recognized a measure of autonomy in the Indian bands and tribes. Treaties rested upon a concept of Indian sovereignty . . . and in turn greatly contributed to that concept."[100] Therefore, up through the 1870s, the United States explicitly and repeatedly recognized tribal sovereignty through treaty making as tribes agreed either to remove to the west of the Mississippi or to cede portions of their ancestral homeland in the face of advancing settlement.[101]

While the formal existence of the United States began at a point in time when the prevailing policy recognized tribal sovereignty through the treaty-making process, such an orientation was not permanent. Once most tribes had either been removed west of the Mississippi River or confined to significantly diminished reservation lands, responsibility for Indian affairs, along with the authority to negotiate on a government-to-government basis with the tribes, moved from the War Department to the Interior Department.[102] Treaties still had to be ratified, and funded, by Congress. In the 1870s, however, Congress ceased making treaties with the Indians[103] and in-

98. *See, e.g.*, Treaty with the Creeks, *supra* note 97; Treaty with the Kaskaskia, *supra* note 97; Treaty with the Western Cherokees, *supra* note 97; Fort Laramie Treaty, Apr. 29, 1868, 15 Stat. 635, *reprinted in* PRUCHA, *supra* note 97, at 109 [hereinafter Fort Laramie Treaty 1868].

99. *See, e.g.*, Treaty with the Six Nations of October 22, 1784, 7 Stat. 15, *reprinted in* PRUCHA, *supra* note 97, at 4; Treaty of Fort McIntosh of January 21, 1785, 7 Stat. 16, *reprinted in* PRUCHA *supra* note 97, at 5; Treaty of Fort Laramie, September 17, 1851, 11 Stat. 749, *reprinted in* PRUCHA, *supra* note 97, at 84 (referring to the United States and the Sioux collectively as "the aforesaid nations").

100. FRANCIS PAUL PRUCHA, AMERICAN INDIAN TREATIES: THE HISTORY OF A POLITICAL ANOMALY 2 (1994).

101. *See, e.g.*, Treaty of Dancing Rabbit Creek, Sept. 27, 1830, 7 Stat. 333, *reprinted in* KAPPLER, *supra* note 97, at 310 (titled "Treaty with the Chocktaw, 1830) (signed by Choctaw leaders at *bok chukfi ahithac*— "the little creek where the rabbits dance"—providing for the removal from the ancestral homelands in Mississippi and Alabama to land in southeastern Oklahoma); Fort Laramie Treaty 1868, *reprinted in* PRUCHA, *supra* note 97, at 109 (signed by the Sioux Nation at the conclusion of the Powder River War, establishing a reservation).

102. *See* VINE DELORIA, JR. & CLIFFORD M. LYTLE, AMERICAN INDIANS, AMERICAN JUSTICE 113 (1983).

103. Treaty making with the Indians was ended by Congress in 1871: "[H]ereafter no Indian nation or tribe within the territory of the United States shall be acknowledged or recognized as an independent, nation, tribe, or power

stead developed a policy of allotting tribal lands to individual Indians,[104] characterizing the allotment program as a "mighty pulverizing engine"[105] that would destroy tribalism and force Indians to assimilate into dominant society as individuals.[106]

If the policy objective of the Allotment Act was to improve the lives of the Indians, it was a colossal failure. By the 1930s, it was clear that the United States needed to change its stance on tribal sovereignty again,[107] and Congress passed the Indian Reorganization Act of 1934 ("IRA").[108] In an effort to reinforce tribal sovereignty, the legislation allowed tribes to adopt constitutions and to reestablish structures for governance.

Of particular interest was the provision in the IRA that allowed tribes to form corporations. While securities law reform was happening simultaneously, it appears that those involved in the IRA had little or no substantive interaction with those involved in the Securities Act of 1933 or the Securities Exchange Act of 1934.[109]

Post-IRA federal treatment of the tribes was less restrictive, allowing for the popular election of tribal leaders accord-

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with whom the United States may contract by treaty . . . ." Abolition of Treaty Making, 16 Stat. 544, 566 (1871), *reprinted in* PRUCHA, *supra* note 97, at 135.

104. General Allotment Act of 1887, 24 Stat. 388 (1887). The statute is also known as the Dawes Act after Senator Henry L. Dawes of Massachusetts. While the Dawes Act represented the final, full-scale realization of the allotment policy, many treaties made with western tribes from 1865 to 1868 provided for allotment in severalty of tribal lands. *See* ROBERT WINSTON MARDOCK, THE REFORMERS AND THE AMERICAN INDIANS 212 (1971).

105. In an address to Congress in 1901, President Theodore Roosevelt expressed his sense of the assimilation policy:

> [T]he time has arrived when we should definitely make up our minds to recognize the Indian as an individual and not as a member of a tribe. The General Allotment Act is a mighty pulverizing engine to break up the tribal mass [acting] directly upon the family and the individual . . . .

Theodore Roosevelt, U.S. President, First Annual Message (Dec. 3, 1901), *reprinted in* 15 COMPILATION OF THE MESSAGES AND PAPERS OF THE PRESIDENTS 6641, 6674.

106. *See* Gavin Clarkson, *Not Because They are Brown, but Because of* Ea*: Why the Good Guys Lost in* Rice v. Cayetano*, and Why They Didn't Have to Lose*, 7 MICH J. RACE & L. 318, 327 (2002).

107. *See, e.g.,* INST. FOR GOV'T RESEARCH, STUDIES IN ADMIN., THE PROBLEM OF INDIAN ADMINISTRATION (1928) (the "Merriam Report"), *available at* http://www.alaskool.org/native_ed/research_reports/IndianAdmin/Indian_Admin_Problms.html (documenting the failure of federal Indian policy during the allotment period).

108. Pub. L. No. 73-383, 48 Stat. 984 (codified as amended at 25 U.S.C. §§ 461–479).

109. For a discussion of the legislative history of the Securities Act, see *infra* Part III.D.

ing to tribal laws and constitutions.[110] Although Congressional policy had completely reversed itself by 1934—tribal sovereignty was now to be encouraged rather than destroyed—federal Indian policy oscillated through one more cycle in the next half century[111] before President Nixon issued a landmark statement calling for a new federal policy of "self-determination" for Indian nations.[112] By "self-determination," President Nixon sought "to strengthen the Indian's sense of autonomy without threatening his sense of community."[113] Self-determination[114] led to an increase in economic development activity, but access to capital remained an impediment.[115] President Reagan also made an American Indian policy statement on January 24, 1983, declaring his support for "self determination."[116] In attempting to give definition to "self-determination," he said:

> Instead of fostering and encouraging self-government, federal policies have, by and large, inhibited the political and

110. RUSSEL LAWRENCE BARSH & JAMES YOUNGBLOOD HENDERSON, THE ROAD: INDIAN TRIBES AND POLITICAL LIBERTY 209 (1980).

111. The period between 1945 and 1970 is referred to as the Termination Era, and was characterized by the passage of number of statutes that "terminated" individual tribes—"these acts distributed the tribes' assets by analogy to corporate dissolution and afforded the states an opportunity to modify, merge or abolish the tribe's government functions." *Id*. at 132. Examples of this legislative activity include Act of Aug. 13, 1954, ch. 732, 68 Stat. 718 (Klamath), Act of Aug. 3, 1956, ch. 909, 70 Stat. 963 (Ottawas).

112. Message from the President of the United States Transmitting Recommendations for Indian Policy, H.R. Doc. No. 91-363, 91st Cong., 2d Sess. (July 8, 1970); *see also* The Indian Financing Act of 1974, Pub. L. No. 93-262, 88 Stat. 77 (1974) (codified at 25 U.S.C. §§ 1451–1453). Perhaps the greatest of Nixon's contributions to Indian tribal sovereignty was Public Law 638, the Indian Self-Determination and Education Assistance Act of 1975, Pub. L. No. 93-638 (codified as amended at 25 U.S.C. §§ 450 to 458bbb-2 (2006)), which expressly authorized the Secretaries of Interior and Health and Human Services to contract with, and make grants to, Indian tribes and other Indian organizations for the delivery of federal services.

113. Samuel R. Cook, *What is Indian Self-Determination?*, 3 RED INK (1994), http://faculty.smu.edu/twalker/samrcook.htm.

114. The key legislation of this era includes: the Indian Self-Determination and Education Assistance Act of 1975, 25 U.S.C. §§ 450 to 458bbb-2 (2006); the Indian Civil Rights Act of 1968, 25 U.S.C §§ 1301–1341 (2006); the Indian Financing Act of 1974, 25 U.S.C. § 1451–1544 (2006); and the Indian Child Welfare Act of 1978, 25 U.S.C. §§ 1901–1963 (2006). *See generally* COHEN 1982, *supra* note 93, at 188–204.

115. *See* COHEN 2005, supra note 90, §21.03.

116. PRESIDENTIAL COMMISSION ON INDIAN RESERVATION ECONOMIES, REPORT AND RECOMMENDATIONS TO THE PRESIDENT OF THE UNITED STATES PART I, at 7 (1984).

> economic development of the tribes. Excessive regulation and self-perpetuating bureaucracy have stifled local decision making, thwarted Indian control of Indian resources and promoted dependency rather than self-sufficiency.[117]

In 1983, President Reagan established the Presidential Commission on Indian Reservation Economies. In 1984, the Commission published its *Report and Recommendations*, again calling for a major shift in federal Indian policy.[118] The Commission promulgated recommendations in the following five categories: Development Framework, Capital Formation, Business Development, Labor Markets, and Development Incentives.[119] Pertinent to the instant inquiry, under Capital Formation, the Commission recommended privatizing tribal enterprise ownership and management, amending the Securities Act of 1933 to place tribes on the same footing as state and local governments, amending the Tribal Tax Status Act to provide tribes with the same tax exemptions as state and local governments, establishing an Indian Venture Capital Fund, amending the Indian Loan Guaranty Fund and the Indian Finance Act to minimize the role of the BIA, and encouraging the private sector to invest in Indian country.[120]

Although some scholars resist the notion that tribes should change in order to participate in the modern capitalist economy,[121] tribes have adapted to their environments for millen-

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117. *Id.*
118. *See id.*
119. *Id.* at 25.
120. *Id.* at 39–47.
121. *See, e.g.*, Robert A. Williams, *Documents of Barbarism*: *The Contemporary Legacy of European Racism and Colonialism in the Narrative Traditions of Federal Indian Law*, 31 ARIZ. L. REV. 237, 266–68 (1989). Professor Williams criticizes the IRA and the notions of evaluating tribal corporations using westernized norms of corporate performance because such evaluations often highlight perceived differences between economic development in Indian Country and corporate America. He also takes issue with the description of tribal structures contained in the PRESIDENTIAL COMMISSION ON INDIAN RESERVATION ECONOMIES, REPORT AND RECOMMENDATIONS TO THE PRESIDENT OF THE UNITED STATES (1984):

> As illustrated by its derogatory nomenclature for describing tribal governments's differences ("social welfare driven"; "patronage system"; "dependent"), the Commission's discourse of tribal self-determination clearly devalues tribal enterprises operated by tribal governments according to tribal values . . . The Commission's point of reference for assigning negative values to contemporary tribalism's perceived self-determining vision of economic development is of course the dominant society's profit driven norms. Thus, if tribalism further declines in re-

nia, and the arrival of Europeans did not diminish that adaptiveness. In fact, many tribes pride themselves on their ability to adapt: the Navajos developed a thriving weaving industry using wool from sheep brought over by Europeans; the Plains Indians incorporated European horses into their culture; and the Choctaw claim that if the Europeans had brought aluminum foil with them, Choctaws would have been cooking with it while the other tribes were still regarding it with suspicion.[122]

The evidence from the last century of tribal economic development indicates that Indian Country can and must compete within the larger capitalist environment, and given a level playing field, they can thrive. With the competitive landscape stacked against Indian Country, however, those impediments are highly suspect if they continue to exist with little or no legitimate purpose, given that they suppress tribal economic development and curtail Indian Country's access to capital.

III. BUSINESS FORMATION IN INDIAN COUNTRY

One area where Indian Country must compete is community economic development, which enables community members to rise out of poverty through the establishment of a stable economy, with small businesses, new jobs, and an entire system structured to support its people. Community economic development has the dual mission of causing positive social impact and achieving financial objectives. The social goal is to achieve financial self-sufficiency for as many in the lowest income population as possible by bringing greater access to financial services.[123] Community economic development can take many forms, but in Indian Country, the first step is often microfinance. Section A introduces the most common source of microfinance lending in Indian Country, the Community De-

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> sponse to the federal government's failure to adequately fund its trust responsibility to Indian people, tribalism's own stubbornly held difference from the superior values of the dominant society will be blamed.

Williams, *supra*, at 267–68.

Irrespective of whether one views capitalism as good or bad, however, the reality is that tribal nations exist within a larger capitalist system, and any assumption that tribes cannot adapt to that system runs the risk of falling into the very discourse that Williams decries.

122. Gavin Clarkson, *Reclaiming Jurisprudential Sovereignty: A Tribal Judiciary Analysis*, 50 U. KAN. L. REV. 473, 502 (2002).

123. RACHEL ROCK ET AL., ACCION INTERNATIONAL PRINCIPLES AND PRACTICES OF MICROFINANCE GOVERNANCE (1988), *available at* http://www.uncdf.org/mfdl/readings/ MFGovernance.pdf.

velopment Financial Institution, or CDFI. Section B then provides some examples of CDFI investments. Microfinance can only take startup enterprises so far, however, and the next level of capital access is usually lacking in Indian Country. Section C describes equity funds, which are often the best source of expansion capital. As mentioned earlier, however, federal securities laws, discussed in Section D, generally preclude tribes from investing in such funds.

A. CDFIs as Catalysts for Business Formation

One of the main ways for communities to develop their economies is through the creation of local community lending funds in the form of CDFIs. In 1994 the Reigle Community Development and Regulatory Improvement Act of 1994 created the CDFI Fund.[124] The CDFI Fund is a wholly-owned governmental corporation that uses the CDFIs as an avenue to promote economic revitalization and community development.[125] Its mission is to "increase the capacity of financial institutions to provide capital, credit, and financial services in underserved markets," through investment in and assistance to CDFIs.[126] The CDFI Fund's creation resulted in a dramatic growth in CDFIs in the 1990s.[127]

Since 2001, Indian tribes have been part of the target market for CDFI Fund assistance.[128] In its Native American Lending Study published in 2001, the CDFI Fund investigated barriers to lending and investment in tribes.[129] The findings led the Fund to create programs and to help tribes build more native CDFIs ("NCDFIs")[130] as well as support those NCDFIs

124. *See* CDFI Overview, http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=7 (last visited Feb. 24, 2009).

125. MARCUS LAMB ET AL., RECOMMENDATIONS FOR CDFI PERFORMANCE MEASUREMENT: IMPROVING MEASURES, INCREASING KNOWLEDGE, BUILDING CAPACITY 2 (2002).

126. Rules & Regulations, 68 Fed. Reg. 23 (Feb. 4, 2003).

127. NAT'L COMM. CAPITAL ASS'N, COMMUNITY DEVELOPMENT FINANCIAL INSTITUTIONS (CDFIS): BRIDGES BETWEEN CAPITAL AND COMMUNITIES IN NEED 5 (2001).

128. Nat'l Tribal Just. Resource Center, CDFI Fund Native American Initiative, *available at* http://www.tribaljusticeprograms.com/funding/fundingdetails.asp?59.

129. *Id.*

130. The Native American segment of the CDFI Fund is the Native Initiative, and its programs include the Native American CDFI Technical Assistance (NACTA) Component of the CDFI Program, the Native American CDFI Development (NACD) Program, the Native American Technical Assistance (NATA) com-

that already existed.[131] As of June 2004, the CDFI Fund had certified twenty-eight emerging or existing NCDFIs.[132] The Fund believed that the increase in number of CDFI institutions and the building of CDFIs' capacity were critical to improving business development in native communities around the United States.[133] In fact, some labeled CDFIs as anchor institutions in Indian economic development.[134] NCDFIs deliver high-quality, culturally relevant business development training and technical assistance to Native Americans who wish to create and build businesses on their reservations.[135]

Another entity, the CDFI intermediary, is often critical to the development and growth of CDFIs in many sectors. First Nations Oweesta Corporation, an affiliate of First Nations Development Institute, is the first and only NCDFI intermediary in the United States. Its mission is "to enhance the capacity of Native tribes, communities, and peoples to access, control, create, leverage, utilize, and retain financial assets; and to provide appropriate financial capital for Native development efforts."[136] By assisting in the creation of native-based institutions that work directly with community members, Oweesta has helped develop alternative financing access for native entrepreneurs, homebuyers, and tribal businesses since the mid-1980s.[137]

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ponent of the CDFI Program, and the Native American CDFI Technical Assistance Program. The NACA and NATA programs award technical assistance (TA) and financial assistance (FA) grants to Native CDFIs and entities that can be certified as Native CDFIs at the time of the award, as well as TA grants to organizations, which can become Native CDFIs within two years. The NACD Program provides TA grants to organizations that sponsor the creation of separate legal entities that will become Native CDFIs. *See* Notice of Funds Availability (NOFA) Inviting Applications for the Native American CDFI Assistance Program, 68 Fed. Reg. 67,906 (Dec. 4, 2003), *available at* http://edocket.access.gpo.gov/ 2003/pdf/03-30174.pdf (federal register announcement); *see also* CDFI Coalition, Native American Programs, http://cdfi.org/index.php?page=advocacy-3a-4 (last visited Feb. 1, 2009) (describing the history of the program).

131. *See* Notice of Funds Availability (NOFA) Inviting Applications for the Native American CDFI Assistance Program, 68 Fed. Reg. 67,906 (Dec. 4, 2003).

132. JENNIFER MALKIN ET AL., NATIVE ENTREPRENEURSHIP: CHALLENGES AND OPPORTUNITIES FOR RURAL COMMUNITIES 37 (2004), *available at* http://www.nwaf.org/Content/Files/Native_Entrepreneurship1.pdf.

133. *Id.* at 39.

134. *Id.* at 53.

135. *Id.* at 55.

136. First Nations Oweesta Corp., Oweesta EITC Fact Sheet, *available at* http://www.oweesta.org/sites/oweesta.org/files/eitcfactsheet.pdf.

137. First Nations Oweesta Corp., About Us, http://www.oweesta.org/about (last visited Nov. 14, 2008).

While Oweesta does not yet offer loans directly to entrepreneurs, the organization enables tribes to prepare their nations to receive funding and assists individuals in investing in native economic development. The corporation researches barriers to native control of access to financial assets and promotes a policy favoring asset building in native communities.[138]

Oweesta's primary focus is on the creation of NCDFIs.[139] In 1999, only two NCDFIs existed in the United States; by 2006 the number was up to thirty-nine.[140] Oweesta empowers tribes to develop their economies by educating members, giving presentations to tribal councils, and training tribal citizens in economic development.[141] Tribes are at different stages in their development, and Oweesta offers individualized support to each tribe seeking help.[142]

The Oweesta Collaborative ("OC") is one of Oweesta's programs. Made up of nine partners, the project encompasses an entrepreneurship development system for the growth of private business on three Indian reservations—the Pine Ridge, Wind River, and Cheyenne River Indian Reservations. [143] The OC project uses both volunteer and paid professional service providers, coaches, and mentors to answer questions and personally assist native entrepreneurs with one-on-one business advice.[144]

B. Examples of CDFI Activity in Indian Country

The Lakota Fund is a NCDFI for the Oglala Lakota Nation in South Dakota.[145] Located on the Pine Ridge Indian Reservation, the Lakota Fund began in 1986 and loaned over

138. First Nations Oweesta Corp., Research, Policy & Advocacy, http://oweesta.org/ps/research (last visited Nov. 14, 2008).

139. Press Release, First Nations Oweesta Corp., Oweesta Introduces New Model for Native Community Economic Development and Offers Training Opportunities (Dec. 6, 2007), *available at* http://www.ournativecircle.org/node/247.

140. First Nations Oweesta Corp., Expanding Native Opportunity: Native Communities Financing Initiative, *available at* http://www.oweesta.org/sites/oweesta.org/files/NCFIBrochure.pdf.

141. First Nations Oweesta Corp., Training, Technical Assistance & Consulting, http://www.oweesta.org/ps/training (last visited Nov. 15, 2008).

142. *Id*.

143. Press Release, First Nations Oweesta Corp., The Oweesta Collaborative: W.K. Kellogg Foundation Awards $2 Million for Regional Entrepreneurship Initiative (May 10, 2005).

144. *Id*.

145. First Nations Oweesta Corp., The Lakota Funds, http://www.oweesta.org/oc/profiles/tlf (last visited Nov. 15, 2008).

$1,000,000 to nearly 300 tribal members for small business and micro-enterprise development.[146] Lakota Red Nation, owned by artist Kelly Looking Horse, is one such business.[147] Looking Horse, a drum-making specialist, began with a $500 loan from the Lakota Fund in 1999 to help establish good credit.[148] From there, he borrowed other small loans, repaying each one before borrowing the next, with the biggest being $5000 in 2006.[149] Looking Horse hopes to one day build a studio and crafts cooperative, but these businesses will require a much bigger loan.[150]

In another example, the Four Bands Community Fund ("FBCF") began in April 2000 with the mission to enable entrepreneurs on the Cheyenne River Indian Reservation.[151] The fund offers training, business incubation, and access to capital, all to build and strengthen reservation-based businesses.[152] JTR Trips is one such business. Three siblings purchased this sporting goods store in Eagle Butte, South Dakota, with the help of the FBCF, as well as the Small Business Administration, Small Business Development Center, and American State Bank in Pierre, South Dakota.[153] Without this assistance, the business might have been moved out of the community.[154]

Eagle Eye Espresso and Tanning, owned by Trina Lends His Horse, used the FBCF assistance to purchase a cash register and inventory.[155] Opening in 2006, Eagle Eye is a drive-up shop offering drinks, food, and a stand-up tanning booth.[156] Business has been quite successful, and Lends His Horse is considering a future business expansion.[157]

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146. *Id.*

147. Oweesta Collaborative, Another Highlight—Success Story for: The Lakota Funds 1, *available at* http://www.oweesta.org/sites/oweesta.org/files/lakred nation.pdf.

148. *Id.*

149. *Id.*

150. *Id.*

151. First Nations Oweesta Corp., Four Bands Community Fund, http://www .oweesta.org/oc/profiles/fbcf (last visited Nov. 15, 2008).

152. *Id.*

153. Oweesta Collaborative, Another Highlight—Success Story for: Four Bands Community Fund, *available at* http://www.oweesta.org/sites/oweesta.org/files/ jtrtrips.pdf.

154. *Id.*

155. Oweesta Collaborative, Another Highlight—Success Story for: Four Bands Community Fund, *available at* http://www.oweesta.org/sites/oweesta.org/files/ trina.pdf.

156. *Id.*

157. *Id.*

The Wind River Development Fund ("WRDF") provides entrepreneurs and businesses on the Wind River Indian Reservation with small business training, counseling, and loans.[158] NATCO, Inc. is one of the businesses aided by the Fund. Floyd Addison, owner and operator, borrowed money from WRDF to purchase a new truck for his business.[159] With his truck and his business acumen, Addison landed a subcontract for a large highway construction project. His business has grown into eleven full-time jobs.[160]

Heyteyneytah, Inc. is another WRDF success story. Stan Addison developed a unique horse-breaking method that does not use force and can be used from his wheelchair.[161] With a small business loan from the Fund, Addison was able to rebuild some of his corrals. He now employs two full-time and ten part-time employees.[162]

Each of these businesses received essential supportive services—monetary and technical—from the NCDFIs. Small loans are vital for starting and building these native enterprises. When the businesses thrive and outgrow themselves though, entrepreneurs need bigger funding sources to enable them to expand their organizations according to demand.

Several NCDFIs have made a tremendous difference in their local communities, but their capacity for providing expansion capital is limited. Successful Indian Country businesses cannot rely solely on CDFIs to increase their businesses, and often bank financing is either unavailable or not appropriate for business expansion.[163] In such instances, businesses need infusions of equity in order to expand.

C. The Role of Private Equity in Business Development

An investment fund is "a business entity whose only important asset is its capital and whose primary business purpose

158. Wind River Development Fund, http://wrdf.org (last visited Nov. 14, 2008).

159. Oweesta Collaborative, Another Highlight—Success Story for: Wind River Development Fund NATCO Inc., *available at* http://www.oweesta.org/sites/oweesta.org/files/natco.pdf.

160. *Id*.

161. Oweesta Collaborative, Another Highlight—Success Story for: Wind River Development Fund Heyteyneytah, Inc., *available at* http://www.oweesta.org/sites/oweesta.org/files/Heyteyneytah.pdf.

162. *Id*.

163. CDFI, *supra* note 27, at 31–32.

is to acquire securities or other assets in the hope that they will appreciate."[164] Such a fund is an independently managed, "dedicated pool[ ] of capital" focused on equity investment in privately-held companies expecting high growth.[165] A private-equity fund is one type of investment fund.[166] Private-equity funds are usually organized as a private partnership or closely held corporation.[167]

Before a private-equity fund invests in a company, careful due diligence is done.[168] Investors play a role in screening, financing, and overseeing the companies in which they invest.[169] Often they are actively involved in the company as a board member.[170]

A private-equity fund has a predetermined lifespan[171] with the intent to complete an investment cycle in ten to thirteen years.[172] For the first five years, money is invested in the company; then it is monitored for several years.[173] Three to seven years after the original investment, the resulting investment is sold.[174] Nearly all venture funds are crafted this way, designed to be self liquidating and end in dissolution.[175]

Private-equity funds generally raise capital from a limited number of sophisticated investors in a "private placement,"[176] which is a form of securities offering that is exempt from registration under the Securities Act. Profits are then split among the professionals administering the private-equity fund and the capital investors.[177]

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164. Robert C. Illig, *What Hedge Funds Can Teach Corporate America: A Roadmap for Achieving Institutional Investor Oversight,* 57 AM. U. L. REV. 225, 268 (2007).

165. PAUL A. GOMPERS & JOSH LERNER, THE VENTURE CAPITAL CYCLE 11 (1999).

166. Illig, *supra* note 164, at 269.

167. National Venture Capital Association, The Venture Capital Industry—An Overview, http://www.nvca.org (last visited Nov. 15, 2008).

168. JOSH LERNER, VENTURE CAPITAL AND PRIVATE EQUITY: A CASEBOOK, at ix (2000).

169. *Id*. at xi.

170. JACK S. LEVIN, STRUCTURING VENTURE CAPITAL, PRIVATE EQUITY AND ENTREPRENEURIAL TRANSACTIONS 1-3 (Martin D. Ginsburg & Donald E. Rocap eds., 2007).

171. GOMPERS & LERNER, *supra* note 165, at 8.

172. LEVIN, *supra* note 170, at 1-3.

173. *Id*.

174. *Id*.

175. LERNER, *supra* note 168, at 12.

176. LEVIN, *supra* note 170, at 1-3.

177. *Id*.

D. Relevant Federal Securities Laws

One main characteristic of private-equity funds is their lack of regulation under federal securities laws.[178] Because they opt for investment in private equity and not publicly traded securities, private-equity firms can avoid most of the costly regulations of federal laws[179] by structuring their activities to fall within the scope of Reg D.[180] Thus these companies want to sell securities only to accredited investors because only then are they assured of being in complete compliance with the securities laws.[181] In contrast, selling to non-accredited investors creates "significant legal complexities and business risks which increase the costs of raising capital."[182] Hence, accredited investor status is the desired category for private-equity firm participation.

The notion of accredited investor is not new, as the current regime of securities regulation in the United States has its origins in the legislative aftermath of the stock market crash of 1929. Though many states had securities laws in effect at the time of the crash, these proved ineffective against the empty promises made by sellers of securities to unsuspecting investors.[183] Of the $50 billion in new securities offered in the 1920s, an estimated half—$25 billion—was lost.[184]

In response to the shattered market, Congress drew together what became the Securities Act of 1933. The purpose of a new federal securities law, declared Representative Sam Rayburn of Texas, was "to place the owners of securities on a parity, so far as is possible, with the management of the corporations, and to place the buyer on the same plane so far as available information is concerned, with the seller."[185]

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178. Illig, *supra* note 164, at 269.

179. Douglas G. Smith, *The Venture Capital Company: A Contractarian Rebuttal to the Political Theory of American Corporate Finance?*, 65 TENN. L. REV. 79, 134–35 (1997).

180. Steven E. Hurdle, Jr., *A Blow to Public Investing: Reforming the System of Private Equity Fund Disclosures*, 53 UCLA L. REV. 239, 246 (2005).

181. CLARKSON, FALKSON, RUBIN & HILLABRANT, *supra* note 22, at 1–2.

182. *Id*. at 1.

183. 77 CONG. REC. 2910, 2931 (1933) (statement of Rep. Wolverton), *reprinted in* 1 J.S. ELLENBERGER & ELLEN P. MAHAR, LEGISLATIVE HISTORY OF THE SECURITIES ACT OF 1933 AND SECURITIES EXCHANGE ACT OF 1934 (2001).

184. The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation, www.sec.gov/about/whatwedo.shtml (last visited Nov. 15, 2008).

185. 77 CONG. REC. 2910, 2918 (1933), *reprinted in* ELLENBERGER & MAHAR, *supra* note 183.

To accomplish this overarching purpose, legislators drafted the securities law with two objectives in mind: to provide investors with financial and other material information about the securities being offered for sale and about the sellers of those securities, and to prohibit deceit, misrepresentation, and other fraud in the sales of securities.[186] By requiring the provision of the information, the lawmakers believed investors would be safer. According to Representative Mapes of Michigan, the Securities Act "will make available to the public the information upon which the public is asked to invest its money."[187]

When considering what types of securities to regulate, Congress determined that some types did not require regulation under the new law. For example, lawmakers perceived "no practical need" for the application of the Securities Act to governmentally issued securities.[188] Governmental bonds were considered sound, and therefore, to avoid unnecessary interference with the course of business, Congress exempted them from the securities law.[189] In the lawmakers' opinion, the government's securities did not need Federal Trade Commission oversight.[190]

During the hearing before the Committee on Interstate and Foreign Commerce in the House of Representatives, other non-governmental entities also found themselves exempt from the new law.[191] Railroad companies, common carriers, and public utilities already subject to federal regulation or supervision on the issue of securities were eliminated from the regulation requirements of the new securities law.[192] Likewise, securities of national banks and Federal Reserve banks were exempt because they already had adequate supervision.[193]

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186. The Investor's Advocate, *supra* note 184.

187. 77 CONG. REC. 2910, 2912 (1933), *reprinted in* ELLENBERGER & MAHAR, *supra* note 183.

188. H.R. REP. NO. 73-85, at 5–6 (1933), *reprinted in* 2 J.S. ELLENBERGER & ELLEN P. MAHAR, LEGISLATIVE HISTORY OF THE SECURITIES ACT OF 1933 AND SECURITIES EXCHANGE ACT OF 1934 (2001).

189. *Hearing Before the Comm. on Interstate and Foreign Commerce, 73rd Cong., 1st Session, on H.R. 4314: To Provide for the Furnishing of Information and the Supervision of Traffic in Investment Securities in Interstate Commerce*, 73rd Cong. 108 (1933), *reprinted in* ELLENBERGER & MAHAR, *supra* note 188.

190. *Id*. at 29.

191. *Id.*

192. *Id.*

193. *Id*.

Nearly fifty years later,[194] the federal government would define these non-governmental exempt organizations as "accredited investors" and place them under the "safe harbor" of Reg D, added in 1982.[195] Thus, from the very beginning, federal and state governments and their instrumentalities were exempt from the securities laws. Indian tribal governments, however, were not exempt under any category.

Despite major reform in Indian policy under the IRA[196] occurring contemporaneously with securities reform, it appears that those involved in the IRA had little or no substantive interaction with those involved in the Securities Act of 1933 or the Securities Exchange Act of 1934. The legislative history of the Securities Act of 1933 makes no mention of tribal governments as serious contenders for the list of governmental bodies exempt from federal securities regulation, nor does it include tribes in the non-governmental groups that were later to become accredited investors. American Indians did get brief mention in the discussion of the Act's creation, albeit perversely. During the discussion in the House about the bill, Representative Sam Rayburn of Texas at one point expounded on the fortitude and ingenuity of European settlers in Virginia:

> The first permanent settlement of English-speaking people in Virginia was accomplished through a joint-stock company. The successors of these early Colonies, through a series of amazing adventures, have wrested a continent from the aborigines, have explored and utilized its natural resources until more than a hundred million people comprise the citizenship of this Republic. The initiative, self-reliance, inventive genius, organizing ability, and industry of the people who have occupied this continent have created a national wealth of some $300,000,000,000.[197]

194. One year after the creation of the Securities Act of 1933, Congress passed the Security Exchange Act of 1934. This act established the Securities Exchange Commission (SEC), which took the place of the Federal Trade Commission in the regulation of securities. The SEC was given the power to register, regulate, and oversee brokerage firms, transfer agencies, and clearing agencies, as well as the nation's stock markets. *See* The Investor's Advocate, *supra* note 184.

195. *See* Revision of Certain Exemptions From Registration for Transactions Involving Limited Offers and Sales, Release No. 33-6389, 47 Fed. Reg. 11,262 (Mar. 16, 1982) (codified at 17 C.F.R. § 230.501).

196. *See supra* text accompanying notes 107–109.

197. 77 CONG. REC. 2910, 2916 (1933), *reprinted in* ELLENBERGER & MAHAR, *supra* note 183.

Rayburn continued with the theme of defeating the "aborigines" with another indirect reference, this time presumably to show the importance of the individual investor: "The conquest of this continent was made by individual human beings, each pursuing his own happiness in his own way."[198]

IV. THE POLICY RATIONALES FOR TREATING TRIBES AS ACCREDITED INVESTORS

For a growing number of American Indian-sponsored venture capital and private-equity firms that are seeking to raise funds from prosperous American Indian Tribes, the practical effect of tribes being defined as "non-accredited investors" is to eliminate this important source of funding. Since these private-equity firms are mission-driven to reinvest their raised capital back into Indian Country business projects, the net effect of tribes being deemed non-accredited is to inhibit capital formation and investment in Indian Country.

A. Wealthier Tribes Should Not Be Excluded from Investment Opportunities that Are Limited to Accredited Investors

In general, not being explicitly mentioned in the list of accredited investors can lead to exclusion from all sorts of investment opportunities, including private-equity funds. While some tribes are poor and have simple structures, others are complex agglomerations of tribal government and tribally-owned non-profits, corporations, and limited liability companies chartered under tribal,[199] state,[200] or federal[201] law.

Just like other entities, tribes with growing, substantial investment assets should have the ability to select from a variety of investment choices to determine the investment portfolio that best meets their needs. Large, well-diversified investors have recently generated some of their best investment returns from private alternative investments such as venture capital,

198. *Id.*

199. *See, e.g.*, Kickapoo Traditional Tribe of Texas, Limited Liability Company Ordinance (n.d.) (on file with author).

200. Tribes can charter a corporation in any state, not just the state that surrounds their reservation. State chartering of a corporation, however, can present problems if the corporation wishes to act as an instrumentality of the tribe.

201. Section 17 of the IRA created a special category of tribal corporation. *See* 25 U.S.C. § 477 (2000).

private equity, hedge funds, and private real estate investment trusts, all such investments requiring accredited investors.[202] Lack of the "accredited investor" designation excludes tribes from participating in these investment categories.

Tribes are unique in that they often embody both governmental and business elements and thus must consider financial needs over varying time horizons. Some investments demand short-term liquidity, while other investments are made for the next seven generations.[203] Many tribes have kept cash not immediately needed in low-earning but safe investments, such as Treasury bonds and certificates of deposit.[204] Tribes not diversifying into higher-earning investment portfolios are not keeping pace with comparable investors. For those tribes with sufficiently large assets, prudent portfolio diversification would include privately-placed investments as a component of overall tribal investment strategy. Based on the discussions that took place at the Economic Summit, a few wealthy tribes have tens or hundreds of millions of dollars to invest and should be able to put a reasonable allocation into higher-earning investments that require accredited investor status, just as other wealthy and institutional investors do. Those tribes increasingly have hired highly educated finance and investment staff who, in turn, oversee external financial advisors and participate in larger and larger deals.[205] In one instance, a tribe was able to outbid three private-equity funds in a corporate acquisition valued at nearly $1 billion.[206] If tribes can compete for investments sought by funds requiring accredited investors, then they should also be able to invest in funds requiring accredited investors.

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202. The market collapse in the fall of 2008 notwithstanding, several of these types of funds have significantly outperformed the market over the past ten years. Since these investments are not registered securities, they routinely limit their investors to those that are accredited investors.

203. A tribe's payroll account, for example, needs to be liquid, while a tribal permanent fund that endows scholarships for tribal youth can be invested in less-liquid investments that generate a higher return than money market funds or certificates of deposit.

204. In my own work with tribes, I have often seen that the history of tribal governments having been taken advantage of dramatically increases the risk aversion of tribal councils when it comes to investment management.

205. *See, e.g.*, *Building a Stronger Tribal Community*, WINDS OF CHANGE, Autumn 2008, at 52 (profiling Bill Lomax, portfolio manager for the San Manual Band of Mission Indians).

206. The Seminole tribe outbid three private-equity firms and acquired the Hard Rock restaurant chain for nearly $1 billion. *Indians To Buy Out Hard Rock*, N.Y. POST, Dec. 7, 2006, at 44.

B. Including Tribes as Accredited Investors Would Enhance Federal Revenues

Given the high levels of unemployment throughout Indian Country, labor market constraints do not exist, and thus presently unemployed individuals will likely fill any jobs created by businesses backed by private-equity investments. Those individuals will pay income and social security taxes, and their employers will contribute additional payroll taxes. A sound economic model should clearly demonstrate the positive federal revenue impact of the increased economic activity if tribes are allowed to deploy capital as accredited investors via private-equity funds. Such a finding would still hold even without factoring in the reduction in welfare transfer payments that result from increased employment and increased per capita income.

Conversely, maintaining the current exclusion of tribes from accredited investor status has a negative impact on federal tax revenues. Since these restrictions keep otherwise viable businesses from being funded with private equity, the federal treasury is missing tax revenues that would otherwise be generated in the absence of these restrictions. Sound fiscal logic and the obvious policy imperative strongly suggested that the SEC should amend Reg D to include tribes.

As an illustration, consider a fictional golf course that an Indian Country entrepreneur would like to develop.[207] If the entrepreneur can raise $5 million to develop the golf course, the ongoing operations will generate more than $200,000 per year in federal income taxes from employees. The positive federal revenue impact would be even greater if the increased level of employment also resulted in a reduction in welfare transfer payments.

The entrepreneur has two basic choices: debt or equity. Non-mortgage bank debt typically requires repayment over a short time horizon (that is, five to seven years at the most), whereas equity money stays in until a "liquidity event" happens, such as the sale of the business. For an individual entrepreneur, unless he has a significant personal balance sheet,

207. A variation of this model was first presented to the Senate Finance Committee during a hearing on May 23, 2006. *See Clarkson Testimony*, *supra* note 49, at 8–10. Based on information from a 2002 report from the University of Georgia, annual payroll is estimated at $1,350,000 and other operating expenses are estimated at $300,000. *See* GA. AGRIC. EXPERIMENT STATIONS, UNIV. OF GA., REVENUE PROFILE OF GOLF COURSES IN GEORGIA (2002), *available at* http://pubs.caes.uga.edu/caespubs/ES-pubs/RR687.pdf.

debt financing is not an option, so the only remaining option is equity. If, however, the entrepreneur cannot raise the capital from private-equity sources, the project will likely not happen. The wages would not be generated, and the concomitant increase in federal revenues would never materialize. Given the number of tribes that would pursue similar projects with expanded tax-exempt bonding authority, the lack of such authority costs the federal government millions of dollars each year.[208]

C. The Proposed SEC Rule Change

No principled reason exists to deny tribal governments the same exempt status that the federal and state governments enjoy, nor the accredited investor status of those currently listed in Reg D. Now, seventy-five years after first designating certain bonds as exempt; more than twenty-five years after the formal creation of the "accredited investor" label; and after many months of interactions with the SEC and other federal officials, including the development and circulation of a working paper that was the precursor to this article, the SEC has determined that it is time to add Indian tribes to the list of accredited investors. In its proposed Revision of Limited Offering Exemptions in Regulation D, the SEC states:

> [W]e propose to amend the Rule 501(a)(3) list of legal entities so that it includes any corporation (including any nonprofit corporation), Massachusetts or similar business trust, partnership, limited liability company, Indian tribe, labor union, governmental body or other legal entity with substantially similar legal attributes.[209]

D. Comments on the Proposed Regulation D Change

During the comments period for the proposed rule change, several individuals and organizations submitted comments on

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208. In *Tribal Bonds*, I estimated that the annual federal tax revenue loss is more than $80 million. These figures do not include other federal revenue savings, such as those associated with reductions in federal entitlement payments resulting from increased employment levels. Clarkson, *Tribal Bonds*, *supra* note 26, at 1074 n.280.

209. Revisions of Limited Offerings Exemptions in Regulation D, 72 Fed. Reg. 45,116, at 45,126 (proposed Aug. 10, 2007) (to be codified at 17 C.F.R. pts. 200, 230, 239).

the SEC's intent to include Indian tribes as accredited investors, all of which were positive. The comments praised the SEC's decision to enable tribes to participate in investment markets on an equal footing with other governments[210] and added further suggestions.

Multiple comments cited the need for a definition of "Indian tribe" to avoid confusion and provide certainty as to which native groups would be included in the SEC's list.[211] One comment suggested that individually naming groups, such as Indian tribes, was too specific,[212] while another commenter was in favor of a finite, more specific list.[213]

Ultimately tribes were added to the definition of accredited investors without opposition. I did express one concern, however, about tribes being listed separately as a accredited investors rather than being listed as governmental entities, which under the proposed rule changes were also included as accredited investors. In particular, I noted

> Tribal governments and their instrumentalities are, like state and local governments, in fact "governments." The Federal government has long recognized Indian tribes under both Federal statutes and long-established legal precedent. For example, the Internal Revenue Code enables Indian tribes and their governmental instrumentalities to issue tax-exempt municipal bonds. Since the proposed changes add a definition of the term "governmental body" to

210. *See, e.g.*, Comment from Stephanie McGillivray & Charles W. Johnson, SOAR Growth Capital, L.L.C. 2 (Oct. 9, 2007), *available at* http://www.sec.gov/comments/s7-18-07/s71807-32.pdf.

211. *See, e.g.*, Comment from Karen Tyler, President, North Am. Sec. Adm'rs Ass'n, Inc., to Nancy M. Morris, Sec'y, U.S. Sec. & Exch. Comm'n 15 (Oct. 26, 2007), *available at* http://www.sec.gov/comments/s7-18-07/s71807-57.pdf (arguing that SEC should clarify the meaning of "Indian tribes"); Comment from Joe Garcia, President, Nat'l Cong. of Am. Indians, to Steven G. Hearne, Special Counsel, U.S. Sec. & Exch. Comm'n 2 (Jan. 2, 2008), *available at* http://www.sec.gov/comments/s7-18-07/s71807-63.pdf (arguing that SEC should define "Indian tribe" to include federally- and state-recognized tribes); Comment from Gavin Clarkson, Assistant Professor, Univ. of Michigan, to Nancy M. Morris, Sec'y, U.S. Sec. & Exch. Comm'n (Oct. 9, 2007), *available at* http://www.sec.gov/comments/s7-18-07/s71807-29.htm (arguing that federally recognized tribes should be included as governmental bodies).

212. Comment from Keith F. Higgins, Lawrence A. Goldman, & Ellen Lieberman, Section of Business Law, American Bar Association, to Nancy M. Morris, Sec'y, U.S. Sec. & Exch. Comm'n 8 (Oct. 12, 2007), *available at* http://www.sec.gov/comments/s7-18-07/s71807-52.pdf.

213. Comment from the Financial Services Group of Katten Muchin Rosenman L.L.P. to Nancy M. Morris, Sec'y, U.S. Sec. & Exch. Comm'n 3 (Oct. 9, 2007), *available at* http://www.sec.gov/comments/s7-18-07/s71807-35.pdf.

> Rule 501(a), similar to the definition of that term that appears commonly in transactional financing, the most appropriate place to include "Indian tribes" is within the list of entities embodied in this definition. Therefore, given the nature of the proposed rule change, I would suggest including "federally recognized American Indian tribes or their instrumentalities" in the list of entities included within the definition of "governmental body" under Rule 501(a). I recommend that only "federally recognized American Indian tribes or their instrumentalities" be included. This limitation, while admittedly excluding some tribes that for reasons of history are not currently recognized by the federal government, does provide a bright line rule for clarity in the markets as to what tribal entities can be an accredited investor.
>
> In summary, "federally recognized American Indian tribes" are governmental bodies and therefore should not be specifically called out in the main text (i.e., under Rule 501(a) (3)), just as states are not called out in the main text. Instead, "federally recognized American Indian tribes and their instrumentalities" should be included in the list of entities recognized as "governmental bodies."[214]

President Joe Garcia of the National Congress of American Indians later echoed this point, although NCAI took the position that state-recognized tribes should also be included.[215] In either case, the point is to emphasize that tribes are, first and foremost, governments.

E. Relation to State Blue Sky Laws

For any proposed change in federal securities law, an examination of the corresponding state securities laws is appropriate because, in addition to the federal statutory scheme, each state has its own body of securities law, dubbed "blue-sky laws."[216] Several states model their laws on one of the versions

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214. Comment from Clarkson, *supra* note 211.

215. Comment from Garcia, *supra* note 211, at 2.

216. This phrase "originated from a depiction of the type of scheme the laws were intended to prevent; that is 'speculative schemes which have no more basis than so many feet of "blue sky." ' " Jay H. Knight & Garrett P. Baker, *Kentucky Blue Sky Law: A Practitioner's Guide to Kentucky's Registrations and Exemptions*, 34 N. KY. L. REV. 485, 486 (2007) (quoting Hall v. Geiger-Jones Co., 242 U.S. 539, 550 (1917)). According to the SEC, state blue sky laws "are designed to protect investors against fraudulent sales practices and activities. While these laws can vary from state to state, most states [sic] laws typically require companies making

of the Uniform Securities Act, drafted by the National Conference of Commissioners on Uniform State Laws. The most recent draft from 2002 has been enacted by fourteen states and the Virgin Islands.[217]

States had their securities laws in place prior to the passage of the federal Securities Act of 1933. In fact, the original intent of the federal law was not to interfere with the state blue-sky laws but to supplement them[218] and to ensure their observance across state lines.[219] At the time that the Act was adopted, Representative Mapes said, "Anything that this Congress can do to supplement the blue-sky laws of the States to protect the public in investing its money ought to be done."[220] In light of the 1929 market crash, state securities statutes were considered inadequate protection for investors.[221] Therefore, the federal bill would preserve the jurisdiction of states' securities commissions to regulate within the states, while itself regulating securities across state lines.[222]

Over time the state supplemental focus of the federal Securities Act changed, resulting in the National Securities Markets Improvement Act ("NSMIA") of 1996. With NSMIA Congress preempted much of state securities laws with respect to federally covered securities.[223]

Federally covered securities no longer fall under the regulatory power of the states. State laws have not been rendered nullities, however. States can still investigate and enforce their antifraud and deceit laws[224] as well as police unlawful broker/dealer conduct in securities transactions.[225] They also

small offerings to register their offerings before they can be sold in a particular state. The laws also license brokerage firms, their brokers, and investment adviser representatives." U.S. Securities and Exchange Commission, Blue Sky Laws, http://www.sec.gov/answers/bluesky.htm (last visited Nov. 17, 2008).

217. Uniform Securities Act: Enactments, http://www.uniformsecuritiesact.org/usa/DesktopDefault.aspx?tabindex=3&tabid=69 (last visited Dec. 5, 2008).

218. Some concern was voiced on whether such a federal law was in error, a usurpation of the reserved police powers of the state and a confusion of state and federal law that would lead to the failure of state law. *See* 77 CONG. REC. 2910, 2938–39 (1933), *reprinted in* ELLENBERGER & MAHAR, *supra* note 183. In a way, such did happen, sixty-three years later, with the passage of the National Securities Markets Improvement Act of 1996, which preempted much of state law.

219. *Id*. at 2912.

220. *Id*.

221. *See id*. at 2930–31.

222. *See id*. at 2918.

223. UNIF. SECURITIES ACT § 102 cmt. 9 (2005), *available at* http://www.law.upenn.edu/bll/archives/ulc/securities/2002final.htm.

224. *Id*.

225. *Id*.

retain the power to require filings of documents with the SEC for notice purposes.[226] Securities exempt under Regulation D of the 1933 Securities Act are federally covered, and that coverage includes accredited investors. Therefore, securities sold to accredited investors do not fall under the regulatory powers of the states.[227]

CONCLUSION

Since there is no principled reason to exclude tribes from the list of accredited investors, this Article in its prior incarnation as a working paper, was instrumental in persuading the SEC to change Regulation D to include tribes as accredited investors. Anticipating the finalization of this change, a number of tribes have expressed an interest in learning more about private equity, as evidenced by the inclusion of private equity as part of the agenda of a number of tribal finance conferences.[228] Once tribes are treated as accredited investors, private-equity funds focused on deploying capital in Indian Country can solicit funds from wealthy tribes. Once Wall Street sees the tribes investing, they will follow with additional investment capital, and Indian Country will have moved past the private-equity tipping point. Although the three private-equity funds[229] that have surfaced thus far will only make a small dent in the $44 billion private-equity deficit, their ability to cherry-pick the best investment opportunities will, in turn, produce significant double-digit returns, which will, in turn, entice other private-

226. *Id.*

227. *Id.* at § 202(14) cmt. 15 (stating that "Section 18(b)(4)(D) of the Securities Act of 1933 defines as federal covered securities those issued under Securities and Exchange Commission rules under section 4(2) of the Securities Act. This would include Rule 506, which uses the 'accredited investor' definition in Rule 501(a). When a transaction involves Rule 506, section 18(b)(4)(D) further provides 'that this paragraph does not prohibit a state from imposing notice filing requirements that are substantially similar to those required by rule or regulation under section 4(2) that are in effect on September 1, 1996' ").

228. *See, e.g.*, Information Management Network, Native American Finance Conference February 2008 Agenda, http://secure.imn.org/~conference/web_confe/index.cfm?sc=20080226_PF_0001&pg=Agenda; NAT'L CTR. FOR AMERICAN INDIAN ENTERPRISE DEVELOPMENT, RESERVATION ECONOMIC SUMMIT & AMERICAN INDIAN BUSINESS TRADE FAIR 2009 AGENDA, http://www.ncaied.org/downloads/RES_2009_Agenda.pdf; Native American Finance Officers Association, Spring 2008 Conference Agenda, http://www.nafoa.org/pastEvents.php.

229. Native American Capital, Native Capital, and SOAR Private Equity have all announced the formation of their initial private equity funds.

equity funds to consider Indian Country as a profitable emerging market.

The Reg D problem is not the only barrier to capital market access for Indian Country. I have previously written about the discrimination against tribes in terms of their tax-exempt bonding authority, but the BIA loan guarantee program is authorized to guarantee tribal bonds,[230] which would provide a similar reduction in interest rates to tax-exempt bonds. No enabling regulations have yet been developed, however. Tribal municipal bonds, whether taxable or tax-exempt, are not exempt from securities registration,[231] while non-tribal municipal bonds are exempt. This lack of a securities registration exemption likely leads to a liquidity premium that makes it more expensive for a tribal government to borrow than a similarly situated non-Indian government. Access to banking services on reservations is made more difficult because of the McFadden Act Amendments to the National Bank Act, which prevent banks that want to do business in Indian Country from opening a branch without the permission of the governor of the state that encompasses the reservation. While these issues will be addressed in subsequent articles, for the moment the prospect of the change to Regulation D that treats tribes as accredited investors is a significant victory.

230. *See* Indian Financing Act, 25 U.S.C. § 1497 (2000).
231. *See* Securities Act of 1933 § 3(a)(2), 15 U.S.C. § 77c (2006).