

Before the
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Committee on Natural Resources

Oversight Hearing on Diversifying Native Economies

Statement of

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Thank you, Chairman Rahall and Ranking Member Young, for the invitation to appear before you. My name is Jonathan Taylor and I am a Research Associate of The Harvard Project on American Indian Economic Development and a Senior Policy Associate with the Native Nations Institute for Leadership, Management and Policy, part of the Morris K. Udall Center for Studies in Public Policy at the University of Arizona.

THE CHALLENGE

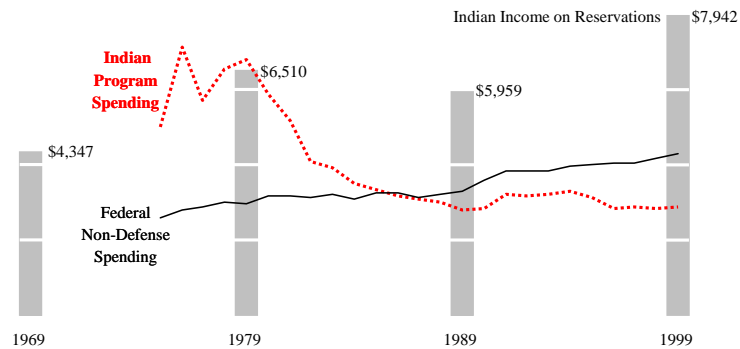
As you are aware, American Indian and Alaska Native economic fortunes have lagged substantially behind those of other Americans. On reservations and in remote rural Alaska, especially, unemployment is high, poverty is high and incomes are low. Declining federal funding, remote markets, challenges attracting educated members, barriers to capital investment, and a host of other problems frustrate Native economic growth.

Nonetheless, bright spots are visible in and around Indian Country. There are places where natural resource companies support education programs. There are places where tourism attracts customers to on- and off-reservation businesses. There are places where tribes manage, regulate, and adjudicate commerce on-reservation better than other governments do. Such was the case before the advent of widespread casino development at the Colorado River Indian Tribes' Farms, at White Mountain Apache's Sunrise Ski Resort, at NANA's Red Dog Mine, and at Mississippi Choctaw's Chahta Enterprise. Such has also been the case after casinos gave tribes additional sources of funds and lowered their costs of capital.

By tribal design, these economic endeavors aim to loose the bonds of federal spending on reservation economies. In the 1970s federal Indian spending rose with the Great Society and other programs, and in the 1980s it fell with the Reagan budget cuts (dotted red line in Figure 1). At the time, much of reservation economic life depended

upon federal grants and contracts, and in synch, Indian incomes rose by 49% in the 1970s, but then dropped by 8% as federal funds retreated in the 1980s (shaded bars in Figure 1). In the 1990s, by contrast, federal Indian spending stagnated and fell behind US spending per capita (solid line in Figure 1), yet Indian incomes grew by a third—three times faster than the US income growth rate. Interestingly, Indian incomes grew on reservations that did *and* did not witness the development of casino gambling.

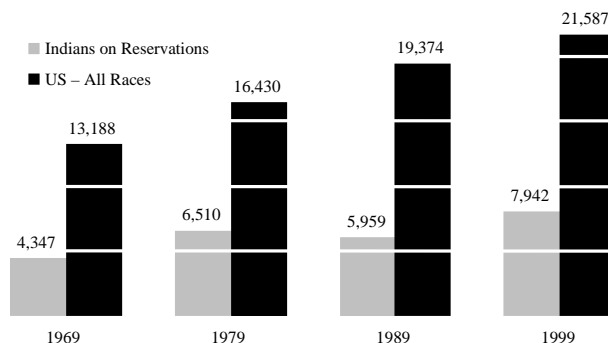
Figure 1
Federal Expenditure Per Capita and Indian Reservation Income
 thousands of 1999 dollars per capita



(Walke, 2000; Taylor & Kalt, 2005)

As welcome as these gains were for Indian Country, Indians on reservations still faced a very large income gap. The gray bars of Figure 1 juxtaposed in Figure 2 against US averages show Indian incomes barely reached past one-third the national average in 1999. Even at the hopeful pace of growth witnessed in the 1990s, it would take fifty-five years for the gap to close, and sustaining that relatively rapid rate of growth for the next half century will be a challenge.

Figure 2
Indian Reservation and National Income
 thousands of 1999 dollars per capita

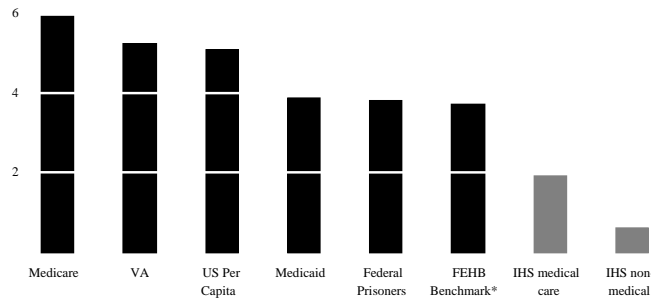


[taylor kalt 2005]

Indians confront these income gaps with weak federal support. Notwithstanding federal treaty obligations and trust responsibilities to advance tribal wellbeing, the US Commission on Civil Rights finds federal funding to be inadequate and below what is

available to non-Indians.¹ The Commission examines a range of domains of Indian life including education, crime, and health, among other things, and finds funding gaps across the range. A particularly stark comparison of health care expenditures is reproduced in Figure 3 and shows Indian Health Service medical funding to be about half of what federal prisoners receive. Given that in Indian Country many social and economic problems have accumulated over time and reinforced each other, one might reasonably expect that reaching social and economic parity with the rest of the US would require greater than average federal funding, not less.

Figure 3
Health Care Spending: Indian vs. Other US
 thousands of FY03 dollars per person



(US Commission on Civil Rights, 2003, Figure 3.2)

Thus, the steep challenge ahead for reservation economies entails accelerating the pace of growth so that the income gap closes in fewer than fifty-five years, all while contending with lower-than-average federal support. The task will require spreading the nascent economic success in Indian Country across industries and across geography. To drive growth, Native economies have relied upon natural resource endowments, upon powers of regulation and taxation, and recently, upon procurement advantages. There is still some room for growth under each of these strategies, but in many reservations, there is not enough to accommodate the number of high-school age workers entering the work force each year. Further growth will have to come from competing head-to-head in value-adding industries and from freeing private sector initiative, especially on large reservations. Success will need to spread geographically, too. Just as mineral resource wealth is concentrated at Crow or in the NANA region of Alaska, so too is success in gaming, gasoline retailing, and cigarette manufacturing concentrated at Ft. McDowell, Winnebago, and Seneca. Economic growth needs to spread over the map as well as through industry sectors.

So how do we deepen and extend the economic success that has been achieved? My colleagues and I at the Harvard Project on American Indian Economic Development and the Native Nations Institute have been learning from Indian Country that there are three essential keys that distinguish tribes in takeoff from tribes that struggle with economic development. First, successful tribes assert, defend, and use their sovereignty. If tribes make the key decisions about development, those decisions tend to better reflect local conditions, preferences, and opportunities; consequently, those decisions yield better tangible results. Second, successful tribes have strong institutions that: a) resolve

disputes fairly; b) manage the boundary between business and politics effectively, and c) administer the day-to-day life of the tribal government efficiently. Without working institutions, economic development can only last a cycle or two of investment, at which point the costs of doing business on the reservation exceed the value and capital flees elsewhere. Third, these institutions of governance must match local norms of what is and is not appropriate government. Without a match between indigenous culture and institutions, the life of government becomes riven with questions of legitimacy and progress halts. Successful Indian nations have in common that they turned away from federally sanctioned, project-based, and grant-funded approaches and instead built governing systems that foster development. I will not belabor the full spectrum of these points because my colleagues have covered them in detail before Congress.² Instead, I want to narrow the focus to one issue in particular: managing the boundary between business and politics.

MANAGING BUSINESS & POLITICS¹

Imagine the government owns a business that provides politically popular services that don't make money. Or imagine the government owns a business where a powerful constituency uses the levers of political representation to strengthen its hand against management in a labor dispute. Or imagine the government owns a business that makes money, but a dispute erupts about whether the profits should be reinvested in the business, used to subsidize popular services, turned over to the government treasury, or issued as dividends to citizens. Such questions pitting corporate success against community values are not idle speculation to the owners and managers of AMTRAK, I'm sure. Likewise, these questions feature prominently in the daily lives of myriad tribally owned corporations. Worse, the political bouts that arise from these questions degrade corporate performance if they are not properly addressed.³

Why not privatize? Countries around the world are driving down the government-owned proportion of GDP to around 5%. When they do so, they reap higher profits, lower prices, better service, and better returns on investment. As appealing as these gains might be, tribal governments nonetheless cannot nor, in many instances, should not privatize their tribal enterprises. US tax, procurement, and regulatory policy encourage and even mandate tribal ownership of enterprise. Section 17 of the Indian Reorganization Act of 1934 encourages economic development via federal charters for nation-owned enterprises.⁴ IRS rules shield nation-owned enterprise profits from federal corporate income tax.⁵ Section 8(a) of the Small Business Act offers advantages to tribally owned corporations.⁶ The Indian Gaming Regulatory Act mandates tribal ownership in all but the rarest cases.⁷

Even in the absence of these federal inducements and requirements, government ownership of enterprises would be a sound choice for Native nations to make. Tribal enterprises often depend upon an Indian nation's patrimony—a forest, lake, river, or plain—whose development must take place within tribal cultural and environmental constraints. Private development of such resources often fails utterly, if only because of

¹ This section draws heavily from work that Kenneth Grant and I wrote in (Grant & Taylor, 2007).

the outcry against inappropriate development institutions. In addition, trust land title, Native concerns about property alienation, geographic isolation, relative economies of scale, and a host of other market idiosyncrasies may favor tribal over individual ownership. And finally, it is often the case that the economic unit is and ought to be the whole community. This is particularly evident in shareholder tribes such as under the Osage headright system (or analogously the Alaska Native corporations), but it can also hold true for whole tribes owning all of a fishery, irrigation system, or hotel. Thus, while private enterprise takes hold on many Indian reservations and deserves more support and encouragement, especially considering the large income gap that remains to be closed,⁸ government ownership of enterprise is properly a feature of Indian economic development and will be for some time. The question is: How can tribes create value as efficiently as the private sector while operating within the constraints of government ownership.

The answer hinges on getting corporate governance right. Enron and the Sarbanes-Oxley response illustrate the challenges of corporate governance *without* government ownership. Corporate governance under Indian nation ownership requires another level of care entirely. The problem arises because two competing sets of relationships become mixed and generate role confusion. On the one hand, we generally like our constituents and representatives to be closely connected through elections, correspondence, constituent service, and the like. On the other hand, we like it when the people we put in charge of our hard-earned assets tighten the ship if standards of customer service are slipping or margins are lagging the industry.

When constituents are employees and representatives are directors, all in the same institution—the tribal corporation—roles and relationships become unclear. Say I'm fired from the tribal company and I have a powerful uncle on the tribal council. Should I play "employee" and go through the due process of the corporate personnel grievance system or should I play "constituent" and go through my uncle? Or say I'm a council representative with many constituents on the tribal housing waiting list and the corporation announces a new investment initiative. Should I to play "representative" and expand the housing budget at the expense of the investment or act as "director," focusing on the long-term prospects of the business? Tribal leaders around Indian Country have encountered problems like these in tribal enterprises repeatedly. The questions do not get resolved easily, and if they fester, profitability decays and even collapses.²

Successful tribal governments formally divide business affairs from elected leadership, usually via a chartered board of directors, but it does not simply serve to adopt a charter. I have seen one tribe copy the charter of a very successful company for its own company only to witness utter collapse. Tribal corporate governance requires: a) a firm governing foundation in the constitution of the tribe and related practice; b) a charter and corporate purpose that represent the Indian nation's priorities and

² While the trappings of the foregoing questions are those of tribal councils and tribal housing programs, the underlying dynamic is not Indian *per se*. The imaginings that opened this section apply equally well to tribal enterprises as to AMTRAK, or British Airways before Margaret Thatcher privatized it.

commitments; and c) ongoing reinforcement of a new organizational culture supporting the elements of corporate governance.

STABLE CIVIC GOVERNANCE

Without robust tribal governing institutions, a tribal charter may be a moot point. If, for example, corporate contracts are adjudicated by the tribal council, the enterprise may never attract investors. Or if the tribal council turns over every couple years, the corporate governance system will be perennially at risk of manipulation, if not dismantlement. Corporate governance systems benefit from a civic governance system that provides:

- Staggered council terms or other mechanisms of stability that permit the system of corporate governance to become enshrined in political institutional memory;
- Independent dispute resolution mechanisms that operate fairly and expeditiously to adjudicate contracts, personnel disputes, property rights, and disputes over the corporate charter;
- Well-defined checks and balances so that policy debates come to an end, reflecting accommodation across the branches of government;
- Clear and predictable rules that do not change with the whims of newly elected leaders or narrow majorities; and
- Civil service professionalism that helps create supportive economic policies such as uniform commercial codes or zoning codes and helps guide infrastructure development.

CORPORATE CHARTER AND PURPOSE

To have worth beyond the paper on which it is printed, a corporate charter must make clear the overarching purpose of the corporation and faithfully represent community compromises regarding the distribution of authority between the corporation and the government. All organizations benefit from clear purposes, of course, but tribal experience demonstrates that when tribal corporations exist to advance a deeply held or widely held community aim (aside from profitability, which is understood), their chances of success improve because constituents, representatives, directors, and employees do not choose roles as opportunistically. The charter must also pre-allocate decision-making authorities in a manner supportable by the citizens of the nation. Generally speaking, the more powers that can be allocated to the board of directors, the better; however, the allocation of authority also entails political questions whose answers are shades of gray rather than black and white. At a minimum, the charter must specify who will perform the following tasks:

- Recruit, nominate, hire, pay, and remove directors of the board;

- Set dividends and retained earnings;
- Set, apply, and adjudicate corporate personnel policy;
- Approve limited corporate waivers of sovereign immunity;
- Develop and use trust lands;
- Approve or reject investment decisions; and
- Reports corporate performance data.

THE PRACTICE OF CORPORATE GOVERNANCE

And of course, paper documents do not necessarily govern behavior. For it to work, the charter must become a new way of ordering relationships. That takes leadership, behavioral change, and organizational culture. Once the charter is written, tribal political and corporate leaders need to alter the incentives actors face within the corporate governance system. If not, the centripetal forces confounding government ownership will work to drag performance down. Among other things, successful tribal enterprises:

- Maintain the engagement of their directors;
- Provide regular reporting from the corporation to the owners;
- Enforce conflict of interest rules;
- Limit the day-to-day interference of elected leaders in corporate decisions;
- Train newly elected leaders and newly appointed directors in the system of corporate governance; and
- Evaluate performance throughout the corporate governance system regularly.

CONCLUSION

Closing the income gap in Indian Country and diversifying Native economies will entail tribes working on a variety of strategies simultaneously, including private sector development, individual financial literacy, social program support for workers, and more. Troubleshooting existing systems of corporate governance and developing new ones for tribally owned enterprises will be critical to the portfolio of strategies. Tribal ownership of business shows no signs of waning, yet it poses inherent challenges that must be faced.

The characteristics listed above are shared by the Winnebago Tribe's Ho Chunk, Inc., the Loudon Tribal Council's Yukaana Development Corporation, and other successful tribal companies around Indian Country. Adopting these characteristics does not guarantee the success these companies have had. Business is risky. One does not automatically arrive at good corporate governance via a lock-step process, nor is

balancing political prerogatives against corporate requirements orderly. Nonetheless the challenges of tribally-owned corporate governance should not lead to despair. Tribes have succeeded precisely because they faced the challenges posed by government ownership directly. They took steps to reduce uncertainty and ambiguity in tribal business by managing the boundaries between government and business well. Continuing to diversify and expand Native economies will hinge on more tribes doing so.

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NOTES

¹ (US Commission on Civil Rights, 2003; US Commission on Civil Rights, 2004)

² (Kalt, 2007; Jorgensen, 2006; Lee, 2001; Kalt, 1996)

³ (Jorgensen & Taylor, 2000; Cornell & Kalt, 1992)

⁴ 25 U.S.C. §477.

⁵ US Internal Revenue Service, Revenue Rule 94-16.

⁶ See, e.g., (US GAO, 2006, 3).

⁷ 25 U.S.C. §2701 *et seq.*

⁸ See, e.g., (Cornell, Jorgensen, Record, & Timeche, 2007)