

**Before the  
United States Senate  
Committee on Indian Affairs**

**Hearing on S.519  
The Native American Capital Formation and Economic  
Development Act of 2003**

**Statement of  
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**My name is Eric Henson and I would like to thank you for the opportunity to appear today. I am employed as a Senior Consultant at Lexecon Inc., and I serve as a Research Fellow at The Harvard Project on American Indian Economic Development, both located in Cambridge, Massachusetts.<sup>1</sup> I am a member of the Chickasaw Nation, and hold graduate degrees in economics and**

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<sup>1</sup> Lexecon Inc. is an economics consulting firm with offices in Chicago, IL, and Cambridge, MA. The Harvard Project on American Indian Economic Development is housed at the Malcolm Wiener Center for Social Policy at the John F. Kennedy School of Government, and is affiliated with the Harvard University Native American Program, a University-wide interfaculty initiative. I appear today not as a representative of Lexecon Inc., Harvard University, or the Kennedy School of Government. Further, I have no financial, organizational, or political interest in the proposed legislation.

public policy.

## THE HARVARD PROJECT ON AMERICAN INDIAN ECONOMIC DEVELOPMENT

Since its inception in 1986, the Harvard Project on American Indian Economic Development has focused on how tribes build healthy, prosperous Indian nations.<sup>2</sup> The Harvard Project has always worked closely with tribes and tribal leaders in an effort to gain a better understanding of this complex issue. The Project's co-directors, Professor Joseph P. Kalt, Ford Foundation Professor of International Political Economy at Harvard University, and Professor Stephen Cornell and Dr. Manley Begay, now directing the Udall Center for Studies in Public Policy and the Native Nations Institute at the University of Arizona, respectively, recognized early on that much of American Indian economic development was actually derived from federal programs and policies, and reflected a view that we would later come to call the "Planner's Approach" to economic and community development.<sup>3</sup> This approach treated development as fundamentally a problem of resources and expertise, rather than incentives and institutions. Its prevailing tenet reflected in a litany of federal programs was that Indian reservations were underdeveloped because they lacked access to a

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<sup>2</sup> Our service to Indian Country, much of it administered in conjunction with the Udall Center for Studies in Public Policy at the University of Arizona, includes comparative and case research, *pro bono* advisory services, executive education for tribal leadership, and a tribal governance awards program referred to hereinafter as "Honoring Nations."

<sup>3</sup> With a majority of development resources tied to grant-based projects *de jour*, it is not surprising that effective grant writing has been at a premium and tribal politics have oftentimes revolved around which leaders could most believably promise delivery of "the next big grant." Development in such a scenario allows any random project being funded by the Federal Government to leap ahead of well-planned projects that are not strategically positioned for grant dollars, undermines long-term planning efforts, and shifts energy and attention away from implementing projects once landed. Instead of project implementation and oversight, many of the creative and managerial talents of the Indian nations are wasted in the perpetual scramble to secure the next big grant, to the detriment of projects already funded.

number of the components for development, paramount among them financial capital and technical and managerial expertise.

The widespread and deep failure of the Planner's Approach is well documented, but a number of success stories, some of which have been highlighted in our Honoring Nations awards program, illustrate the innovation and skill Indian nations exhibit in overcoming and moving away from this model. I will briefly mention two well-known examples. First, the Mississippi Band of Choctaw Indians, which began its drive to development lacking abundant natural resources, an ideal location, or a highly experienced workforce. This tribe did, however, have one key raw material B a labor force that was willing to work hard when presented the opportunity. For this Indian nation, this key raw material, when coupled with decades of slow and steady growth, the reinvestment of tribal proceeds, and a consistent vision for the future, has produced a vibrant and diversified economy. From initial investments in the manufacturing sector to a wide range of ancillary services, the Mississippi Choctaw built an economy admirably poised to fend for itself, even in the face of the Federal Government's sometimes-fickle adherence to its trust responsibility.

The second example is that of the Mashantucket Pequot Tribal Nation. Most have heard of the Mashantucket Pequots, as they now receive more attention and press than many would have likely imagined just a few short years ago. I mention them here to provide an example of another highly successful Indian nation that found one key raw material B an excellent location for a gaming operation B and then paired that key material with a development plan

that benefited from this underlying advantageous asset. The rapidity of the success of the Mashantucket Pequots is easily contrasted with Mississippi Choctaw's long, slow development path, but these two nations share a common thread in their rise to prosperity, a thread that bears on the discussion of legislation such as S.519. The similarity between the development paths of the Mississippi Choctaw and the Mashantucket Pequots was a lack of sufficient start-up capital. It is perhaps difficult to believe today, but one of the common experiences these two Indian nations initially encountered was a near total exclusion from the financial markets and the funding necessary to initiate significant tribal development efforts. The Mississippi Band of Choctaw Indians largely overcame these obstacles by starting smaller than it might otherwise have, and by continually reinvesting in its tribal businesses. The Mashantucket Pequot Tribal Nation largely overcame these obstacles by finding overseas investors willing to take a chance on its developmental vision.

To be certain, the lack of capital flows into Indian Country has long been a pervasive problem, even for some of the most successful Indian nations such as the Mississippi Band of Choctaw Indians and the Mashantucket Pequot Tribal Nation. The proposed legislation presents a welcome opportunity to address this challenge head-on. Yet, as over a decade-and-a-half of research and fieldwork conducted by the Harvard Project demonstrates, the problem of inadequate access to capital cannot be treated in isolation. Removing barriers to obtaining capital or increasing the level of capital available to tribes, for example, is unlikely to produce robust development among those Indian economies that lenders and investors in the marketplace deem unsafe places to invest. The fundamental challenge is to create a political and institutional

**environment that attracts capital.**

**The Federal Government can play an important role in sparking economic development in Indian Country not only by improving tribes' access to capital, but also by assisting in tribal efforts to create environments that are conducive to economic development. As noted above, the pairing of these efforts is essential and I am encouraged that S.519, in providing for the diagnosis of the political, legal, regulatory, and investment environments of particular tribes, recognizes the importance of well-functioning institutions in the process of creating the setting for capital formation. To this end, the Harvard Project's research on the institutional bases of economic development may be instructive. I will not belabor them here, but a brief summary is warranted.**

- **Capable Institutions:** Institutions of dispute resolution, business regulation, administrative law, property, taxation, and the like lay down the formal rules of the game that determine rewards and penalties, opportunities and risks. However, governmental infrastructure does not represent the only institutions in a society. Healthy and stable social and cultural institutions complement these more formal bodies, and together the appropriate mix of sound institutions can interact to promote economic development.
- **Cultural Match:** The structure of a society's formal institutions of governance and economic development must be consonant with underlying norms of political power and authority in order for those institutions to function effectively in service to that society.

A nation that has internal agreement as to how it will be governed will create governing organizations that are legitimate in the eyes of the governed, absent some external constraint that prohibits the formation of such bodies.

- **Sovereignty and Self-Determination:** The policies of sovereignty and self-determination, embarked upon in the mid-1970s,<sup>4</sup> underpin the only strategy we have been able to identify that has shown any prospect of breaking the patterns of poverty and dependence that became so familiar to Indian people, particularly on the reservations. A word of caution here, though B these policies are not enough in isolation. Economic development success stories in Indian Country are uniformly marked by (1) aggressive assertions of sovereignty that resulted in (2) self-governed institutions that are characterized by (3) cultural match. Continued *de facto* dependence on other governments= policies and approaches kills accountability for tribal leadership and puts others= norms and values in charge.

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<sup>4</sup> The implementation of these policies has ebbed and flowed since their initiation, with greater consistency being beneficial for the Indian nations as it affords them a clearer understanding of the Arules of the game@ in their planning and operational efforts.

The compelling need to vigorously and proactively support sovereignty and self-determination cannot be overstated. Self-determination aligns the policies of the Federal Government with the proper incentives of the Indian nations themselves, and the appropriate incentives are central to the challenge of economic development. Our research makes it clear, for example, that contracting and compacting, whereby tribes take over the management and delivery of programs otherwise within the domain of the Federal Government (e.g., under PL 638), have been successful in both promoting economic development and enhancing tribes' experience in the business of self-governance. From forestry to health care, the hard, statistical evidence says that tribal takeover of programs is working.<sup>5</sup> Programs administered by tribal institutions (and tribal political leaders) that bear the risks, and simultaneously share the rewards, of development decisions outperform programs that are not characterized by this alignment of incentives. The ownership structure envisioned in S.519 includes a creative capitalization mechanism that appears to be an attempt to align the incentives of the ownership of the proposed Native

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<sup>5</sup> Matthew B. Krepps, "Can Tribes Manage Their Own Resources? The 638 Program and American Indian Forestry" in Cornell and Kalt, *What Can Tribes Do?* (University of California: 1992); Alyce Adams, "The Road Not Taken: How Tribes Choose Between Tribal and Indian Health Service Management of Health Care Resources," Doctoral Dissertation, Harvard University, October 1999; and National Indian Health Board, *Tribal Perspectives on Indian Self-Determination and Self-Governance in Health Care Management*, completed 1998. This research does not indicate that every instance of contracting or compacting is an unqualified success, but it supports the conclusion that self-determination is the only policy that has thus far worked to create viable and sustainable economic development in Indian Country.

American Capital Development Corporation (ANACDC) with the types of policies required to overcome a dearth of capital formation in Indian Country.

**IMPLICATIONS OF THE RESEARCH FOR S.519  
THE NATIVE AMERICAN CAPITAL FORMATION AND ECONOMIC  
DEVELOPMENT ACT OF 2003**

The need for innovative solutions to the problems facing Indian nations is substantial, and legislation such as S.519 can help overcome the obstacles tribes confront today. If one thinks of the three core findings of the Harvard Project as the necessary components to construct the engine of sustained economic prosperity throughout Indian Country, an important question remains: What is the fuel that powers that engine? It is a combination of inputs, such as the labor force of the Mississippi Choctaws or the location of the Mashantucket Pequots, mixed with vision for the future, and complemented by financial expertise and the start-up funds necessary to get Native endeavors off the ground. Notwithstanding the success of certain tribes, and the access to financial markets that such success typically produces,<sup>6</sup> there remains a compelling need to fuel the economic engines of Indian Country.<sup>7</sup>

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<sup>6</sup> For a recent example, see *Mohegans Obtain Credit Facility to Pay Debt Costs on Casino*, *Indian Country Today*, April 16, 2003, at C1. This article explains how the Mohegan Tribal Gaming Authority recently restructured its debt and will use \$391 million in credit to meet its maturing obligations. The restructuring involved a syndicate of 12 lenders, which is led by Bank of America.

<sup>7</sup> A current focus in much of the popular press centers on the lucrative gaming industry, to the detriment of a more complete picture that we have observed in Indian Country. This focus misses at least two fundamental realities: (1) that numerous tribes do not have access to funding remotely approaching the revenue streams (and financial services more broadly) of



**S.519 is an attempt to provide the fuel needed in Indian Country, and as such is a commendable initiative. However, the proposed legislation leaves a number of questions yet to be answered. Examples include:**

- **Organizational Questions: (1) Is the NACDC an initiative of Indian Country, or will it be seen as the Planner-s Approach to the obstacles of capital formation? (2) Is a Congressionally chartered corporation the proper entity to address the market failures inherent in delivering financial services to Indian Country? (3) How will this organization impact and interact with existing entities that attempt to address this problem, including private for-profit businesses, philanthropic foundations, and non-governmental organizations?**
- **Operational Questions: (1) Does the NACDC-s ability to receive appropriations undermine its directive to operate as a self-supporting corporation? (2) Will attempts to address the inapplicability of standard underwriting criteria in Indian Country create a portfolio of unacceptably high risk lending in the Native American financial institutions served by the NACDC? (3) Does inclusion of the Native American Economies Diagnostic Studies Fund and the Native American Economic Incubation Center Fund unnecessarily burden an organization expected to be self-supporting?**

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the most successful gaming tribes; and (2) the fact that a given tribe-s ownership of a successful business venture does not diminish the trust responsibility owed to that tribe.

I am not going to attempt to address these, or similar, questions in detail, but instead I will focus my comments on two conceptual aspects of S.519: the Native American Economies Diagnostic Studies Fund (ADiagnostic Fund<sup>8</sup>) and the Native American Economic Incubation Center Fund (AEconomic Fund<sup>8</sup>).<sup>8</sup> These components of the proposed legislation are particularly noteworthy because they potentially differentiate this organization from some of the now-existing entities that are also attempting to address the lack of capital formation in Indian Country.

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<sup>8</sup> Collectively referred to hereinafter as Athe Funds.<sup>@</sup>

Activities undertaken through the Diagnostic Fund and the Economic Fund<sup>9</sup> present an opportunity to appropriately target efforts of the NACDC toward capacity-building for Indian nations. The NACDC will then join a select few Indian service organizations that strive to build the capabilities of Indian nations to implement self-determined economic development initiatives and, in turn, strengthen the capacities of those nations to exercise their sovereignty in real, meaningful ways. The language of S.519 acknowledges this goal, and the Committee's effort in establishing this organization is testament to the recognition that the level of capital flows has thus far been insufficient. Through the diagnostic and reformative research envisioned, the NACDC will attempt to help establish, tribe-by-tribe, settings into which capital will more freely flow. The tribe-by-tribe, situation-by-situation approach spelled out here is central. Two of the great failings of the Planner's Approach have been (1) the consistent attempt to apply one-size-fits-all legislation to the varied and disparate Indian nations, and (2) the imposition of federal policy onto societies not greatly suited for the policy in question, not prepared to implement programs thus established, and not involved in the formulation of the legislation mandated by the Federal Government.

What does this capacity-building approach entail for a given diagnosis carried out under the auspices of the Funds? As implied above, it is impossible

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<sup>9</sup> I do find that the language pertaining to the Economic Fund, specifically, "The Corporation shall use amounts in the Economic Fund to ensure that Federal development assistance and other resources dedicated to Native American economic development are provided *only* to Native American communities with demonstrated commitments to (A) sound economic and political policies; (B) good governance; and (C) practices that promote increased levels of economic growth and job creation," (emphasis added) should be clarified and greater specificity should be established as the legislation progresses.

to provide a completely general answer B the need to tailor each analysis precludes formulation of an adequate checklist for every situation. However, we have learned a fair amount about the types of developmental infrastructure required for sustainable economic progress. The particular political, legal, regulatory, and investment setting underlying each tribal circumstance will differ in name, relative importance, and functional interaction, but the commonalities observed provide a starting point for the work of the NACDC. While recognizing that the importance of each of the components of a well-functioning economy will vary greatly from tribe to tribe, all are essential to ensure that the providers of capital will maintain the flows of funds required to keep these Indian economies operating. To this end, each diagnostic project should begin with an effort to understand the tribe-s developmental infrastructure, including (but not limited to) the presence and effective implementation of:

- Financial and budgetary controls, such as third-party audits. This maximizes the probability that poor business decisions, or malfeasance, will not undermine commercial activities.
- Sound principles of corporate governance, including the separation of tribal politics from tribal businesses. This maximizes the ability of tribal businesses to succeed in competitive marketplaces.
- Regulatory codes, including land-use ordinances, commercial codes, health codes, housing ordinances, tax provisions, etc. This maximizes the ability of all parties to understand the rules under which business and commercial ventures will operate.
- Planning and development policies, such as strategic plans or visioning documents. This maximizes the likelihood that suitable

foresight and thought will be brought to bear upon development opportunities.

- A separation of powers between the branches of tribal government, including independent tribal courts. This maximizes the possibility that lenders and investors will not be subjected to arbitrary actions that could adversely affect them.
- A tribal Constitution (written or unwritten) supported by the governed. Evidence of broad-based acceptance of the above mechanisms of legal, regulatory and investment infrastructure may be indicated by the presence of a legitimate and effective Constitution.

These all help an economy develop by instilling confidence on the part of outside commercial interests, depoliticizing dispute resolution proceedings, standardizing and streamlining commercial practices and contract enforcement, and enhancing tribal sovereignty by allowing the tribe to exert its regulatory authority over business activity.<sup>10</sup> The net result is increased capital formation and the attendant benefits of expanded employment prospects, higher incomes, and improved standards of living.

I would like to close by noting that there is no need for an Indian nation today, be it the poorest tribe only now embarking on a path for sustainable economic development, or the most prosperous Indian nation, to be arbitrarily and inappropriately excluded from the financial services that are readily

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<sup>10</sup> See Eric Henson and Luxman Nathan *A Tool of Sovereignty: The Crow Commercial Code*, Harvard Project Report Series 98-4 (Harvard Project on American Indian Economic Development: April 1998), and Eric Henson and Luxman Nathan, *Adopting Commercial Codes: Overcoming Lending Barriers on Reservations*, *Communities and Banking*, No. 24 (Federal Reserve Bank of Boston: Winter 1999).

available to other, non-Indian entities. Initiatives such as S.519 can join the gradually growing list of programs thoughtfully reversing the policy mistakes of the past B many of which are so well entrenched as to seem irreversible. To the extent that Indian Country supports S.519, and to the extent that it can help Indian nations overcome the numerous obstacles to capital formation and sustained economic development, it is an initiative that should fully receive the support of this Committee.