TESTIMONY TO THE SENATE COMMITTEE ON INDIAN AFFAIRS

APRIL 30, 2003

HEARING ON S 519

SUBMITTED BY

THE NATIVE AMERICAN BANCORPORATION

The Native American Bancorporation is pleased to have this opportunity to present testimony on S 519 and generally on issues involving capital formation in Indian Country. My name is Derrick Watchman, a member of the Navajo Nation and a member of the Board of directors of the Bancorporation.

In our testimony today, we will provide an introduction to the Native American Bancorporation (NAB), our views on S. 519, some general observations on capital formation in Indian Country and a set of recommendations on steps the Congress and the Federal agencies can take to assist capital formation on Indian reservations. In general, our bias is toward private sector (i.e. Indian originated and controlled) initiatives with appropriate governmental support but minimal bureaucratic involvement.

I. The Native American Bancorporation and its Subsidiaries

NAB is a bank holding company, certified by the Federal Reserve Board that is owned and controlled by twenty-one Tribal Nations and Alaska Native Corporations. The board of directors of NAB is composed of representatives from these investors. Our ten "Founding Tribes", each of which invested $1 million in NAB are:

Arctic Slope Regional Corporation
Blackfeet Indian Nation
Grand Traverse Band Economic Development Corporation
Mandan, Hidatsa and Arikara Nation
Mashantucket Pequot Tribe
Mille Lacs Reservation Business Committee
The Navajo Nation
Oneida Tribe of Indians of Wisconsin
Shoshone Business Council
Ute Mountain Ute Tribe

Senator Inoyue inspired the formation of NAB in the spring of 1997 during a meeting with tribal leaders who were discussing the same challenges to economic development in Indian Country that underpins this proposed legislation. We became a reality in the fall of 2001.

NAB's principal subsidiary is the Native American Bank N.A. (NABNA), a national bank chartered by the Office of the Comptroller of the Currency as a Community Development Focused Bank. NABNA offers a full range of community banking services to the Blackfeet Indian Community through its office in Browning Montana and we are pursuing opportunities to establish similar community banks in other reservation communities. Our executive offices are located in Denver, Colorado and serve as the base for our national market coverage. NAB N.A. offers the full range of banking services to all customers, but with a special focus on serving tribal governments, Alaska Native Corporations, Indian owned businesses and Indian non-profit organizations. The Bank has unique expertise in and sensitivity to the special circumstances involved in lending to tribes and on-reservation businesses – such as tribal sovereignty, the trust status of Indian land, and the use of credit enhancements such as the BIA loan guarantee program and mortgage programs under NAHASDA.

The Bank received its charter from the OCC on September 29, 2001 and opened for business shortly thereafter. We spent the subsequent year building our team and making ourselves known in Indian country. We are now fully operational, making loans, receiving deposits, and providing other services to our customers from all over the country. More than 80% of our new loans are to Indian Country interests. We also recently opened a trust department. Our long-term plans call for the opening of branches on reservations throughout the country and we are working to promote teaming relationships with other existing tribally owned financial institutions. The Bank is certified as a Community Development Focused Institution (CDFI) by the Treasury Department.

In addition to NABNA, NAB is the sponsoring organization of the Native American Community Development Corporation (NACDC) a 501©(3) non-profit corporation. When forming NAB, the tribal leaders of the founding tribes recognized that there were many financial needs in Indian country that could not be met by a for-profit national bank. Many loans that are needed -- for mortgages, for small business, for land acquisition and other purposes --are not bankable, either because the borrower does not meet the eligibility criteria for commercial loans or because the loan will not cash flow at standard interest rates and terms.

In addition, many of these potential borrowers need a substantial amount of technical assistance. Yet these small business loans and mortgage loans are needed in order to improve the economic conditions in Indian country and reduce the poverty that causes banks to reject so many loan requests. In other words, without access to capital through loans there can be no economic development, but without economic development, it is difficult for many prospective borrowers or loans to qualify.

To help break this vicious cycle, NAB created NACDC and gave it seed money to get started. NACDC's mission is three-fold – 1) to serve as a national source of loan funds for loans that will promote reservation development but which NABNA and other banks are not equipped to make, with an emphasis on low income mortgages, start-up businesses, and land consolidation; 2) to break down barriers to credit faced by Indians, particularly those living on reservations and to become a center of expertise for Indian country on innovative approaches for addressing the credit needs on reservations; and 3) to provide financial literacy and other banking education programs to help increase access to banking services for reservation residents. To carry out its mission, NACDC will obtain the bulk of its funding from foundations, Federal grant programs, and large financial institutions' community reinvestment programs.

NACDC's first priority has been to focus on mortgage financing for reservation housing with the long-term goal of creating a source of low-interest funds available to local reservation housing programs for low-income mortgage-financed housing. While it is developing such programs it has already begun working with several tribes and their housing authorities on mortgage financed housing initiatives in which NACDC helps to break down barriers to mortgage financing, to access support from entities such as Fannie Mae, the Federal Home Loan Banks and mortgage finance institutions in order to package mortgage financed housing units on the reservation, and to assist the tribes develop much needed home buyer education programs. While NACDC has been in existence for less than a year, we are extremely excited about the opportunities that we see for a significant increase in mortgage financed housing on reservations through partnerships with NABNA and other private sector lenders.

NACDC's second priority is in the area of providing capital to deal with the issues of fractionated heirship interests and the re-acquisition of reservation land that has fallen into non-Indian ownership. In this area we have teamed with the Indian Land Tenure Foundation (ILTF), which is also testifying today and which will provide detailed information on the initiatives ILTF and NACDC have in mind for this area. Finally, NACDC plans to establish a national re-lending program for micro and startup loans to small businesses in reservation communities. Finally, NACDC is working to increase financial literacy in Indian Country, specifically through the expansion of the very successful Mini-Banks in the Schools Program developed on the Blackfeet Reservation.

II, Our Views on S. 519

NAB strongly supports the objectives of S. 519. There is a critical need to bring focused attention and expertise in order to promote mortgage financed housing on reservations and to tear down the barriers that have limited the amount of mortgage financed units to a trickle, notwithstanding the various Federal programs and commitments from large financial institutions to address this need. It is clear that the problems in this area will not be solved without a concentrated effort.

It is also important that there be resources available to provide tribes with more options for creating sustainable economic development in their communities. Tribal members need good jobs and the prospect of a brighter future in order to break the cycle of poverty endemic in so many reservations. We believe that the best way to facilitate this is through

Indian owned and controlled financial institutions that are responsive to the unique culture and needs in Indian country and the unique legal structure governing trust land.

Significant progress is being made in this area. In addition to NAB, there now exist at least twenty (20) certified Community Development Financial Institutions in reservation communities. Thirty-seven (37) Indian applicants (including NABNA) received grants under the CDFI Fund's NACTA grants program in 2002 and we expect even more activity in this area in 2003. We thank the Committee for its work in supporting this targeted effort to increase economic development activities at the local level.

Unfortunately, while a very encouraging start, the combined capacity of these institutions is a proverbial "drop in the bucket" compared to the realities in Indian Country. Confronted with the very real choices between funding badly needed social services to their members and allocating capital to economic development projects with a long term payback, tribal leaders are forced to make the proper decision of meeting today's needs first. With growing populations and budgets made even tighter by the returns now available on invested funds, investment capital is very hard to find in a reservation economy. We see this almost every day in our banking activities.

With respect to S.519, in the spirit of self-determination and private sector development, we believe that it is preferable for Congress, if it chooses to legislate in this area (and we hope it will), to focus the legislation on ways to strengthen the Indian financial institutions created by the tribes and individual Indians with as much decision-making as possible delegated to the local level. What is needed is access to a source of capital that is more patient and inexpensive that that which is available through private sector sources. In many ways, Congress, and this Committee in particular, have already succeeded in accomplishing many of the objectives of S. 519 through the extensive support and encouragement it provided for the development of financial institutions created by Indian tribes and individuals.

NAB recommends that Congress, the Federal agencies and the Indian community work together to improve the odds of success for those Indian-created institutions that are empowered under existing legislation. This help is critical given the huge unmet capital needs in Indian country. In particular, there is a need to 1) address the land issues of fractionated ownership, checker-boarded reservations and acquisition of ancestral homelands, 2) provide access to equity capital for business formation and expansion, and 3) create a better climate for business opportunity in Indian country, since when real business opportunity exists, capital soon follows - even to Indian reservations - as demonstrated by the Indian gaming industry.

In the view of NAB, it is these three goals that Congress should focus on as it works to address the capital formation needs in Indian country. In turn, we offer our hand in partnership to work with you on them. As a first step, we have set out below our suggestions on some specific actions Congress and the Federal agencies can take to help achieve them. Our primary goal is to increase economic activity and job creation on those reservations and Alaska Native Villages that suffer unemployment rates far in excess of the national average.

III. Recommendations for Increasing Capital Formation in Indian Country

A. Actions that do not require new appropriations

Recognizing that obtaining new appropriations is always a struggle, we would like to begin with steps that can be taken that do not require new Federal dollars but instead make better use of existing dollars or that remove barriers to capital formation on reservations:

1. Provide that certain grant funds be administered by Indian financial institutions.

We ask that Congress review various Federal funding programs to determine if it would be more productive to give those funds to Indian financial institutions, which can leverage them, rather than to Federal agencies that cannot. One example, and Cris Stainbrook of the Indian Land Tenure Foundation will elaborate on it, is the funds Congress provides for the acquisition of fractionated interests. Last year, Congress provided the BIA with $7 million for the Indian Land Acquisition Fund, and the BIA proceeded to use those funds to purchase $7 million in fractionated interests. That is, one dollar in Federal funds purchased one dollar of land.

In contrast, if the funds were instead provided to an Indian Land Tenure Financial Institution of the kind that ILTF and NACDC are hoping to establish, that $7 million could be combined with low-interest loan funds from the Federal Home Loan Banks, regular loan funds from banks such as NABNA, and perhaps matching grant funds from foundations, to create subsidized, long-term, lower interest, land acquisition loans that cash-flow using the income from the land acquired. Through this approach, the $7 million could result in the acquisition of perhaps $70 million in fractionated heirship interests. We believe there are likely many other cases in which Federal funds could be leveraged to accomplish a great deal more if they were in the hands of Indian financial institutions rather than in the hands of Federal agencies.

2. Reduce BIA Red Tape

One of the biggest barriers to the effective flow of capital on reservations is the red tape that is imposed by the BIA in its capacity as trustee. We fully support that trust relationship and are not suggesting that it be diminished. However, we believe that the process can be streamlined so that transactions on reservations more closely resemble those in the private sector. For example, presently, it can take the BIA 6-9 months in some regions to process a title status report or to approve a mortgage. By the time those 6-9 months have passed, the time limit established by the bank for holding the interest rate has expired and the mortgage needs to be renegotiated. The net effect is to discourage prospective lenders because time is money and the extra time required to deal with this red tape or to have to reprocess a mortgage loan can eat up much of their profit.

This is not the proper time to expound on this issue, but NAB urges the Committee to hold a separate hearing on improving the property system on reservations, at which time NAB and NACDC will be pleased to provide some detailed recommendations on ways the red tape can be reduced.

3. Trust Funds

The Department of the Interior manages over $3 billion in Indian trust funds. An issue separate from the trust fund problems that have been discussed and fought over in this room and in the Federal courtroom is the fact that those $3 billion dollars contribute nothing to Indian economic development or capital formation. Meeting the Federal government's trust responsibility and allowing those funds to contribute to economic development are not mutually exclusive. Private financial institutions manage hundreds of billions of dollars in trust for both public and private sector investors. If those trust dollars were similarly managed by Indian financial institutions, those dollars would work for Indian country without in any way diminishing the trust relationship. Four years ago, Chairman Campbell and then-Senator Frank Murkowski introduced a bill, called S 739, which would have permitted tribes, at their option, to have private financial institutions manage their trust funds, under accepted trust standards, without losing the trust status of those funds. The bill provided a preference for Indian-owned financial institutions. Chairman Campbell, NAB urges you to dust off that old bill and re-introduce it. It is more relevant and necessary now than it was when first introduced. It will strengthen self-determination, improve capital formation in Indian country, and strengthen Indian-owned financial institutions.

4. Requiring Federal Capital Formation Programs to Recognize the Unique Situation in Indian Country

Congress has established several different programs to help promote capital formation in low-income communities, including the CDFI Fund and the New Markets Tax Credit Program. However, the criteria these programs use too often have the unintended effect of excluding Indian financial institutions. For example, the first round of the New Markets program was just completed and only one Native American institution received funding and tax credits under it – an Alaska Native entity – and we are thankful for the help. But the reason that only one Native institution benefited is that the criteria placed a heavy emphasis on demonstrated performance. But as indicated earlier in this testimony, most of the financial institutions in Indian country are new and lack the track records to meet these criteria. We urge Congress to direct programs such as New Markets to consider a set-aside for Indian-country that reflects the infancy of the Indian financial institutions.

5. Promoting Business Opportunities

One of the most important steps Congress can take to promote capital formation is to promote business opportunities in Indian country, such as helping to insure that a portion of those Federal contracts that can be performed on reservations are set aside for reservation-based firms. Capital is very mobile and it will flow to solid business opportunities wherever they are located. For example, thanks to the efforts of Senators Inouye and Stevens, $34 million was included in the FY 03 Defense Appropriations bill for a contract to a coalition of ten tribally owned 8(a) information technology firms. A $34 million contract is the kind of asset and business opportunity that attracts capital and, in fact, NAB is presently negotiating a $1million line of credit with that coalition. If Federal agencies were required to direct more such contracts to reservation-based firms, there would be a very rapid flow of capital to those locations, without the need for any new appropriations.

Unfortunately, Congressional pressure is needed to make this happen, even for Indian programs. For example, the Office of Historical Trust Records in the Interior Department is getting ready to award an $18 million contract for the scanning of trust records, many of them located on reservations. Yet that Office is unwilling to make that award in a manner that insures the award will go to reservation-based companies. As a result, the capital created by that contract will flow to Fairfax Virginia or New Delhi, India, rather than to Indian reservations. Congress needs to stop these shortsighted actions by those officials who supposedly are working for the Indian people.

B. Recommendations requiring new appropriations

There are also several steps needed that do require new appropriations. However, all of the steps recommended involve leveraging of the Federal dollars

1.Increase the Size of the BIA Loan Guarantee Program

The BIA loan guarantee program has become a valuable and successful program. NAB and many other banks use it so they can make loans that otherwise would not be bankable. These are good loans; they have to be because the bank is at risk for at least 10% of them. But for so many of the reasons discussed above, the bank cannot make them without a guarantee. The BIA loan guarantee program provides one of the best leveraging opportunities in the Federal budget. There is a need for only $8 in appropriations for every $100 in loans that can be guaranteed. The problem is that the limited funds presently appropriated to that program limit the amount of loans it can guarantee to $68 million. The program has approvable requests for 2-3 times that amount. We urge the Congress to double the ceiling this year and keep raising it in future years so long as there is a need. With 9-1 leverage, it is one of the most cost effective approaches for increasing capital formation in Indian country.

2. An Equity Fund

One of the most glaring deficiencies in Indian country is the lack of access to equity or venture capital for economic development. Financial institutions such as NABNA are senior lenders, not venture capitalists. SBA has a program called the Small Business Investment Company or SBIC program. Under it, SBA will provide four dollars in non-recourse debentures for each private sector dollar invested. An SBIC is permitted to make equity investments in small businesses. It also provides technical assistance to insure that the business it has invested in succeeds. There is a need for a national Indian SBIC, perhaps as part of the NACDC Small Business Intermediary. However, it is difficult to raise private sector funds for such an institution.

We therefore request that Congress create a matching program or challenge grant through a one-time $5 million appropriations. When Indian country raises an equal amount, those dollars would become available for an investment in an SBIC, where the $5 million in appropriated funds for this effort would produce a total of $50 million for equity investments in Indian country (the appropriated $5 million, the matched $5 million and the SBA match of four times that $10 million or $40 million). There is also a need to amend the Small Business Act so the definition of "small business" for the SBIC program parallels the definition in the 8(a) program because the latter has a definition of "small business" that has been tailored to reflect the unique circumstances of tribally owned businesses, while the SBIC program does not.

3. A Feasibility Fund

Another form of capital critically needed in Indian country is non-recourse loans for feasibility and development. NAB has first hand knowledge of the value of such money. Ten years ago, as part of a CRA agreement with the bank regulators, a large bank agreed to create a $15 million fund for non-recourse loans for feasibility and development activities in connection with the creation of minority-owned banks. If the activity produced an operating bank, the loan had to be repaid; if the bank never got off the ground, the loan was forgiven. NAB was a recipient of such a loan and it was critical to its ability to develop the present institution.

There is a need for a similar fund for feasibility studies of new businesses on reservations. Tribes are continually being approached and asked to invest in new business opportunities that can create jobs on reservations. Most tribes lack the ready funds to conduct proper feasibility studies or development activity. As a result, they either reject the opportunity, or in a few cases, make the investment and find that it was infeasible, but only after it has burned up the tribe's investment. If NACDC were provided a one-time grant of $2-$3 million dollars for such a feasibility fund, it believes it could leverage that with grants from private foundations to create a self-sustaining feasibility fund for reservation businesses.

Conclusion

Indian country now has or is planning to create many of the entities and programs needed to address the capital formation gaps on reservations and in Alaska Native villages. While they can facilitate the kind of local decision making that is most effective in steering capital to its highest and best use, what is needed is access to significant amounts of capital on appropriate terms. Also helpful would be a small amount of tailored funding for specialized institutions such as an SBIC and a feasibility fund, expansion of the BIA loan guarantee program, plus a number of non-appropriations actions by Congress to create business opportunity and remove barriers to capital formation. NAB was started through the support and assistance of Senator Inouye and other members of this Committee. It is now eager to assist the Committee in return, by using our banking expertise to work with you to nail down the specific actions needed to improve capital formation in Indian country and to advocate for those actions in Washington and throughout the country. We look forward to working with you on this important endeavor. Thank you for providing NAB with the opportunity to testify.