

Indian Tribes Not Taxed on Section 17 Corporation Income— Even When Earned Outside Indian Country

Chairman Horton is striving to bring clarity to the income tax consequences to Indian tribes operating businesses outside Indian Country.

Many of California's over 100 federally recognized Indian tribes are choosing to operate commercial activities, outside of Indian Country. These activities range from real estate enterprises to technology start-ups. Consequently, this created some uncertainty for the tribes when it comes to income tax consequences.

Recently, we succeeded in working with a California tribe and the Franchise Tax Board to clarify that tribes operating businesses organized as section 17 corporations outside Indian Country are not taxed on the income of the corporation. The following information should be helpful if your tribe operates a section 17 corporation and faces similar confusion about the income tax consequences of the business.

What is a section 17 corporation?

Section 17 of the Indian Reorganization Act of 1934 (IRA) gives tribes the power to organize a federally chartered tribal corporation to engage in business transactions. To form a section 17 corporation, a tribe must draft a charter, submit it for approval to the Bureau of Indian Affairs, and receive an Approval Article or Certificate signed by the Secretary of the Interior. The corporation must be structured as a legal entity wholly owned by the tribe, but separate and distinct from the tribal government.

A section 17 corporation shares the same privileges and immunities as the tribal government, but holds assets or property separately from the tribal governing body. The property or assets of the corporation are at risk in the amount necessary to satisfy creditors and developers; however, property owned by the separate and distinct tribal governmental body is still protected by sovereign immunity and is safe from the execution of a judgment against the corporation.

Is a section 17 corporation's income taxable?

Tribal corporations formed under section 17 of the IRA are not recognized as separate entities for federal tax purposes. The section 17 corporation has the same tax status as the tribe. **The Supreme**

Court case of Mescalero Apache Tribe v. Jones determined states may retain the right to tax tribal corporations; however, California law under Regulation 23038(b)-1(a)(3) treats tribal corporations formed under section 17 as an arm of the tribe (411 U.S. 145 (1973)). Since the tribe is not subject to federal or California income tax, the section 17 corporation is also not subject to federal or California income taxes for income derived from its activities. Therefore, neither the Internal Revenue Service nor the Franchise Tax Board can impose tax on a section 17 corporation's income, regardless of whether the corporation's operations occur inside or outside of Indian Country.

Do you still have questions?

If you have any questions about the California taxation of a section 17 corporation or other tribal tax issues, please feel free to contact Chairman Horton's Franchise and Income Tax Counsel, Ms. Jaclyn Appleby, at 916-445-4154, or email Ms. Appleby at jaclyn.appleby@boe.ca.gov.

As always, we are at your service.