

**OVERVIEW OF FEDERAL TAX PROVISIONS AND ANALYSIS OF
SELECTED ISSUES RELATING
TO NATIVE AMERICAN TRIBES AND THEIR MEMBERS**

Scheduled for a Public Hearing
Before the
SENATE COMMITTEE ON FINANCE
on May 15, 2012

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION



May 14, 2012
JCX-40-12

CONTENTS

	<u>Page</u>
INTRODUCTION AND SUMMARY	1
I. GENERAL RULES REGARDING THE TAXATION OF INDIAN TRIBES AND TRIBAL MEMBERS AND THE TAXING POWERS OF INDIAN TRIBES	3
A. Income Taxation of Indian Tribes and Wholly Owned Tribal Corporations.....	3
1. Federal income taxation of Indian tribes and wholly owned tribal corporations ...	3
2. State taxation of Indian tribes	4
B. Tax Treatment of Enrolled Members of Indian Tribes	7
1. Federal tax.....	7
2. State tax.....	7
C. Taxing Powers of Indian Tribes.....	9
D. Alaska Native Settlement Trusts.....	10
II. SELECTED FEDERAL TAX RULES AND ISSUES RELATING TO INDIAN TRIBES AND THEIR MEMBERS.....	12
A. The General Welfare Doctrine.....	12
B. Indian Tribal Governments Treated as States for Certain Purposes (sec. 7871)	14
1. In general	14
2. Tax-exempt bonds.....	14
C. Gaming Activities of Indian Tribes	21
1. Overview.....	21
2. Federal tax treatment of income from gaming operations	22
3. Treatment of gambling winnings and losses.....	22
4. Wagering excise and occupational taxes	23
D. Economic Development Incentives	26
1. Accelerated depreciation for business property on Indian reservations (sec. 168).....	26
2. Indian employment tax credit (sec. 45A).....	27
3. Empowerment zones (secs. 1393(a)(4) and 1391(g)(3)(E))	28
4. Renewal communities (secs. 1400E(a)(1)(B)(ii), 1400E(a)(5) and 1400E(c)(2)(C)(ii))	29
5. Credit for the production of Indian coal (sec. 45).....	30
E. Exclusion From Income and Employment Taxation of Income Derived by Indians From Exercise of Fishing Rights (sec. 7873).....	31
F. Exemption from Federal Unemployment Tax for Employment by Indian Tribes (secs. 3306(c)(7), (u), and 3309(d))	32
G. Charitable Contribution Deduction for Certain Expenses in Support of Native Alaskan Subsistence Whaling (sec. 170(n))	33

III. BACKGROUND STATISTICS ON NATIVE AMERICANS.....	34
A. Overview.....	34
B. Proportion of Native Americans in the U.S. Population.....	35
C. Geographic Distribution of Native Americans in the United States.....	37
D. Economic Status of Native Americans	39
E. Educational Attainment of Native Americans	44
F. Indian Health Service and Health Status of Native Americans	45

INTRODUCTION AND SUMMARY

The Senate Committee on Finance has scheduled a public hearing for May 15, 2012, entitled, “Tax Reform: What It Could Mean for Tribes and Territories.” This document,¹ prepared by the staff of the Joint Committee on Taxation, provides a description of Federal tax law and an analysis of selected issues relating to Native American² tribes and their members as well as data on the economic status of Native American tribes and Native Americans in the United States.

Native American households generally have lower incomes and higher rates of poverty than other households in the United States. According to 2010 U.S. Census data, the median income of a Native American household was \$35,062, compared to \$50,046 for the U.S. population as a whole. Among those living on Indian reservations and eligible to work, 49 percent were unemployed in 2005; 29 percent were employed but had annual earnings below the poverty line. Overall, 27 percent of Native Americans lived in poverty in 2009, compared to 14 percent for the U.S. white population.

A unique feature of Indian country is that investors doing business in Indian country must contend with three tax systems – Federal, State, and tribal – often with uncertain application. Native American tribes and States both have the power to tax certain transactions of non-members of Native American tribes within Indian country, possibly resulting in double taxation of such transactions and a disincentive to invest in business ventures on reservations.

Part I of this pamphlet provides an overview of the Federal and State taxation of Indian tribes and their members and of the taxing powers of Indian tribes. Indian tribes generally are exempt from Federal income tax and, in the absence of Congressional consent, generally are exempt from State income tax. With limited exceptions, enrolled members of Indian tribes are subject to Federal income tax, but generally are exempt from State income tax unless Congress consents to such taxation. Indian tribes have an inherent sovereign power to tax transactions that occur on certain Indian lands and that significantly involve the Indian tribe or its members. Part I also discusses the treatment of Alaska Native Settlement Trusts established to promote the health, education, and welfare of beneficiaries and to preserve the heritage and culture of Alaska Natives.

¹ This document may be cited as follows: Joint Committee on Taxation, *Overview of Federal Tax Provisions and Analysis of Selected Issues Relating to Native American Tribes and Their Members* (JCX-40-12), May 14, 2012. This document updates Joint Committee on Taxation, *Overview of Federal Tax Provisions Relating to Native American Tribes and Their Members* (JCX-61-08), July 18, 2008. Both documents can be found on the Internet at www.jct.gov. The staff of the Joint Committee also prepared another document for this hearing which provides an overview and analysis of Federal tax laws relating to five U.S. possessions and describes the economies of the possessions. This document may be cited as follows: Joint Committee on Taxation, *Federal Tax Law and Issues Related to the United States Territories* (JCX-41-12), May 14, 2012. This document can be found on the Internet at www.jct.gov.

² The laws regarding Native Americans generally use the term “Indian.” This pamphlet uses the terms Native American and Indian interchangeably. For purposes of this pamphlet, the terms Native American or Indian refer to people having origins in any of the original peoples of the 50 U.S. States and the District of Columbia, unless otherwise stated.

Part II discusses several special rules regarding the taxation of Indian tribes or their members and the taxation of income from certain activities conducted by Indian tribes or on Indian reservations. For example, under section 7871 of the Internal Revenue Code, Indian tribes explicitly are afforded comparable treatment to that of U.S. States for certain purposes under the Federal tax laws. These purposes include, among others, the ability to receive deductible charitable contributions, the ability to issue tax-exempt bonds in certain circumstances and special treatment for purposes of certain Federal excise taxes. Part II also describes tax rules relating to gambling operations, which as indicated above, now produce significant revenue for many Indian tribes. Part II then describes several tax rules, most of which have expired, designed to encourage economic development on Indian reservations, including: (1) accelerated depreciation rules for property on Indian reservations; and (2) the Indian employment tax credit. Part II also describes various other special income and employment tax rules.

Part III provides statistical information regarding Native Americans in the United States, including information concerning the economic conditions and population of Native Americans.

I. GENERAL RULES REGARDING THE TAXATION OF INDIAN TRIBES AND TRIBAL MEMBERS AND THE TAXING POWERS OF INDIAN TRIBES

A. Income Taxation of Indian Tribes and Wholly Owned Tribal Corporations

1. Federal income taxation of Indian tribes and wholly owned tribal corporations

No specific Code³ provision governs the U.S. income tax liability of Indian tribes.⁴ However, the Internal Revenue Service (“IRS”) has long taken the position that Federally recognized Indian tribes and wholly owned tribal corporations chartered under section 17 of the Indian Reorganization Act of 1934⁵ and section 3 of the Oklahoma Indian Welfare Act⁶ are not taxable entities for U.S. income tax purposes and are exempt from U.S. income taxes, regardless of whether the activities that produced the income are commercial or noncommercial in nature or are conducted on or off the Indian tribe’s reservation.⁷ In contrast, a corporation organized under State law and owned by an Indian tribe or tribal members may be subject to U.S. income tax on income earned from activities conducted on or off the Indian tribe’s reservation.⁸ The tax status of tribally owned corporations chartered under tribal law (as opposed to Federal law) has not

³ Unless otherwise stated, all section references are to the Internal Revenue Code of 1986, as amended.

⁴ However, section 7871 of the Code provides that Indian tribes (referred to as “Indian tribal governments”) are treated as States for certain Federal tax purposes. These purposes are discussed in Part II below.

States and their political subdivisions are exempt from tax under an implied statutory immunity in that no provision of the Code imposes a tax on the income of States and their political subdivisions (and no provision expressly exempts such income from tax). In some cases, however, Congress can override this implied immunity as it has done in section 511(a)(2)(B) of the Code, which imposes an income tax on the unrelated business income of State colleges and universities.

⁵ 25 U.S.C. sec. 477.

⁶ 25 U.S.C. secs. 501-509.

⁷ See, e.g., Rev. Rul. 94-65, 1994-2 C.B. 14 (extending Rev. Rul. 94-16 to Oklahoma tribal corporations organized under the Oklahoma Indian Welfare Act); Rev. Rul. 94-16, 1994-1 C.B. 19 (neither an unincorporated Indian tribe nor a corporation organized under section 17 of the Indian Reorganization Act of 1934 is subject to Federal income tax on its income); Rev. Rul. 81-295, 1981-2 C.B. 15 (Federally chartered Indian tribal corporation has the same tax status as the tribe and is not taxable); Rev. Rul. 67-284, 1967-2 C.B. 55 (Indian tribes are not taxable entities); Internal Revenue Service Office of Indian Tribal Governments, *FAQs Regarding Status of Tribes (Taxable vs. Nontaxable vs. Not Subject to Tax)*, available at <http://www.irs.gov/govt/tribes/article/0,,id=102543,00.html>.

Legal commentators generally have concluded that under the “so-called Indian Commerce Clause [article I, section 8 of the Constitution] and Supreme Court cases, there is little constitutional limitation on the ability of the Federal government to tax Indian tribes or tribal members.” Ellen P. Aprill, “Tribal Bonds: Indian Sovereignty and the Tax Legislative Process,” *Administrative Law Review*, vol. 46, 1994, pp. 333, 334. The Supreme Court has never held unconstitutional a Federal tax applied to Indians. See *Lac Courte Oreilles Band of Lake Superior Chippewa Indians v. United States*, 845 F.2d 139, 143 (7th Cir. 1988); *Chickasaw Nation v. United States*, 208 F.3d 871, 880 (10th Cir. 2000).

⁸ Rev. Rul. 94-16, 1994-1 C.B. 19; Rev. Rul. 94-65, 1994-2 C.B. 14.

been addressed by the IRS in published guidance but commentators suggest that the treatment may depend on the extent to which the corporation is an “integral part” of the Indian tribe.⁹

2. State taxation of Indian tribes

In general

Indian tribes and tribal corporations generally are exempt from State taxation within their reservations, and remain so unless Congress clearly manifests its consent to such taxation.¹⁰ For example, the United States Supreme Court held that Congress consented to State *ad valorem* real property taxes on Indian land from which limitations on alienation were removed through the issuance of a fee patent.¹¹ Accordingly, land owned in fee by an Indian tribe is generally subject to State property taxes whether located within or outside of Indian country,¹² even if the land had been formerly held in trust for the Indian tribe.¹³

⁹ Felix S. Cohen, *Cohen's Handbook of Federal Indian Law 2005 Edition*, LexisNexis, 2005, p. 675 (noting that the IRS has issued letter rulings which may not be relied upon as precedent, Private Letter Ruling 200409033, February 27, 2004, and Private Letter Ruling 200148020, November 30, 2001, treating tribally chartered entities the same as the tribe for tax purposes after determining that the entities in question were integral parts of the tribe).

¹⁰ *Oklahoma Tax Commission v. Chickasaw Nation*, 515 U.S. 450 (1995); *Montana v. Blackfeet Tribe of Indians*, 471 U.S. 759 (1985); *McClanahan v. Arizona State Tax Commission*, 411 U.S. 164 (1973); *Cass County, Minn., v. Leech Lake Band of Chippewa Indians*, 524 U.S. 103 (1998) (explained below).

¹¹ *County of Yakima v. Confederated Tribes & Bands of the Yakima Indian Nation*, 502 U.S. 251, 253-56 (1992) (finding a clear manifestation by Congress to permit such taxation in the Indian General Allotment Act of 1887, 25 U.S.C. sec. 331 *et. seq.*, as amended by the Burke Act of 1906, 25 U.S.C. sec. 349).

¹² Land within Indian reservations generally is held either in trust by the Federal government for the benefit of a tribe or individual members of an Indian tribe, or owned in fee by either an Indian tribe, members of an Indian tribe, or non-Indian persons. Initially, Indian reservation land generally was held in trust by the Federal government for the benefit of Indians resident on the land. From the late 19th century until passage of the Indian Reorganization Act of 1934, 25 U.S.C. sec. 461 *et seq.*, the Federal government allotted certain Indian lands to individual members of an Indian tribe and after a period of time issued fee patents to some of the allotted parcels. The recipient of a fee patent was free to sell the land, which has resulted in certain portions of Indian reservations presently being owned in fee by Indians, Indian tribes, and non-Indians. With the passage of the Indian Reorganization Act of 1934, Congress halted further allotments and extended indefinitely the existing period of trust applicable to already allotted, but not yet fee patented, Indian lands. See *County of Yakima v. Confederated Tribes & Bands of the Yakima Indian Nation*, 502 U.S. 251, 253-56 (1992).

¹³ *Cass County, Minn. v. Leech Lake Band of Chippewa Indians*, 524 U.S. 103 (1998). A different case is presented in *Oneida Indian Nation v. City of Sherrill*, 145 F. Supp. 2d 226 (N.D.N.Y. 2001), where lands owned in fee by the tribe were held not to be subject to State property taxes because they were located within Indian country and Congress had not consented to taxation of the lands by the State. The lands in question had never been allotted to individual tribal members, but had been made alienable through a controversial course of conduct specific to the region in which the lands are situated.

Congress has not consented to all taxes on property. States may not apply a property tax to allotted lands held in trust for an Indian tribe by the Federal government, and States may not apply an excise tax upon the sale of any interest in land within an Indian reservation.¹⁴

Income taxes

Indian tribes generally are taxable by States on income earned outside of their reservations.¹⁵ However, any land or right acquired by the United States in trust for an Indian tribe pursuant to the Indian Reorganization Act¹⁶ is exempt from State taxes, even if the land or right so acquired is located outside of a reservation.¹⁷ Income from mineral royalty interests is exempt from State taxation if it is derived by an Indian tribe from the lease of unallotted reservation land and entered into under the Indian Mineral Leasing Act of 1938.¹⁸ Nevertheless, States may apply production taxes to the exploitation of mineral interests by non-Indians pursuant to such a lease, whether or not the value obtainable by an Indian tribe for the mineral lease is affected.¹⁹ However, States may not apply production taxes that are so high as to have a significant negative effect on the marketability of an Indian tribe's product.²⁰

Sales taxes

States may impose sales and excise taxes on sales or activities within an Indian reservation if the legal incidence of the tax rests on persons who are not tribal members, the balance of Federal, State, and tribal interests favors the State, and minimal burdens in collecting the tax are imposed on an Indian tribe or tribal members.²¹ Two cases illustrate the limits of State power to apply a tax upon persons who are not tribal members engaged in business in Indian country. First, a State may not apply a motor carrier license fee or fuel use tax on a non-Indian logging company's use of reservation roads where the logging was pursuant to a

¹⁴ *County of Yakima v. Confederated Tribes & Bands of the Yakima Indian Nation*, 502 U.S. 251, 268-70 (1992).

¹⁵ *Mescalero Apache Tribe v. Jones*, 411 U.S. 145 (1973) (tribe held to be subject to State gross receipts tax on income earned from a ski resort operated by the tribe off-reservation).

¹⁶ Indian Reorganization Act, ch. 576, 25 U.S.C. sec. 461 *et seq.* (1934).

¹⁷ *Mescalero Apache Tribe v. Jones*, 411 U.S. 145, 155-59 (1973). The exemption under the Indian Reorganization Act extends to bar a compensating use tax on personal property permanently attached to realty, but does not bar an income tax or a non-discriminatory gross receipts tax on income derived from a business conducted using the property. *Ibid.* at 158.

¹⁸ *Montana v. Blackfeet Tribe of Indians*, 471 U.S. 759 (1985).

¹⁹ *Cotton Petroleum Corp. v. New Mexico*, 490 U.S. 163, 186-87 (1989).

²⁰ *Montana v. Crow Tribe*, 484 U.S. 997 (1988), summarily aff'g 819 F.2d 895 (9th Cir. 1987), *explained in* *Cotton Petroleum Corp. v. New Mexico*, 490 U.S. 163, 187 (1989).

²¹ *Oklahoma Tax Commission v. Citizen Band Potawatomi Indian Tribe of Ok.*, 498 U.S. 505 (1991) (upholding State cigarette sales tax on sales to non-members of the tribe); *Cotton Petroleum v. New Mexico*, 490 U.S. 163 (1989) (upholding imposition of State severance tax on private producers of oil and gas on reservation lands); *Oklahoma Tax Commission v. Chickasaw Nation*, 515 U.S. 450, 459-60 (1995).

comprehensive Federal regulatory scheme and the roads used were maintained entirely by the Indian tribe and the Federal government.²² Second, a State may not apply a gross receipts tax to a non-tribal member's construction firm that was employed to build a school for an Indian tribe, when the school was to be financed and operated by the Indian tribe and the Federal government.²³

²² *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980).

²³ *Ramah Navajo School Board Inc. v. Bureau of Revenue of New Mexico*, 458 U.S. 832 (1982).

B. Tax Treatment of Enrolled Members of Indian Tribes

1. Federal tax

Ordinarily, individual members of Indian tribes are subject to Federal income taxes, even if the source of the income received by individual tribal members is income distributed by the Indian tribe and otherwise exempt when received by the Indian tribe.²⁴

Certain types of income earned by members of Indian tribes are not subject to Federal tax. One such type is income earned from the exercise of certain fishing rights, explained below in section II.E. Also excluded from tax are payments in satisfaction of a judgment of the United States Court of Federal Claims in favor of an Indian tribe that are distributed per capita to tribal members pursuant to a plan approved by the Secretary of the Interior,²⁵ and per capita distributions made to tribal members from certain Indian trust funds.²⁶ A third type of income excluded is income derived directly from land held in trust by the Federal government for the benefit of an Indian tribe or a member of an Indian tribe.²⁷ Income is derived directly from trust land if it is generated principally from the use of reservation land and resources rather than from capital improvements upon the land, and includes income from logging, mining, farming, or ranching activities.

2. State tax

Individual members of an Indian tribe that reside in Indian country are exempt from State taxes, unless Congress clearly manifests its consent to such taxation.²⁸ Members of an Indian tribe who reside outside of a reservation are subject to State taxes on income, regardless of whether the income was derived from within an Indian reservation.²⁹

As explained above, States may not apply a property tax to allotted lands held in trust for an Indian tribe or members of an Indian tribe by the Federal government, and may not apply an

²⁴ *Squire v. Capoeman*, 351 U.S. 1, 6 (1956). Per capita payments of net revenues from gaming activities conducted or licensed by any Indian tribe are specifically made subject to Federal taxes by the Indian Gaming Regulatory Act, 25 U.S.C. sec. 2710(b)(3)(D), Pub. L. No. 100-497 (October 17, 1988).

²⁵ 25 U.S.C. secs. 1401-1407.

²⁶ 25 U.S.C. sec. 117b(a). A special rule, described below, governs distributions from an Alaska Native Settlement Trust.

²⁷ *Squire v. Capoeman*, 351 U.S. 1 (1956). A number of courts have held that the exclusion is only available for income derived from land allotted to the individual earning the income and is not available for income derived from land leased from the tribe or another individual to whom the land is allotted. *Kieffer v. Comm'r*, T.C. 1998-202; *Anderson v. United States*, 845 F.2d 206 (9th Cir. 1988); *Holt v. Comm'r*, 364 F.2d 38 (8th Cir. 1966); but see *Campbell v. Comm'r*, T.C. Memo 1997-502, at 19. The exclusion does not extend to income derived from the reinvestment of income derived from allotted land. *Capoeman*, 351 U.S. at 9.

²⁸ *Oklahoma Tax Commission v. Chickasaw Nation*, 515 U.S. 450 (1995); *Montana v. Blackfeet Tribe of Indians*, 471 U.S. 759 (1985); *McClanahan v. Arizona State Tax Commission*, 411 U.S. 164 (1973).

²⁹ *Oklahoma Tax Commission v. Chickasaw Nation*, 515 U.S. 450, 462-67 (1995).

excise tax upon the sale of any land within an Indian reservation. However, States may apply real property taxes to property that is owned in fee by an Indian or persons who are not tribal members within reservations. In addition, States may require tribal members to collect sales taxes on sales made to non-members of the Indian tribe.³⁰

³⁰ *Oklahoma Tax Commission v. Citizen Band Potawatomi Indian Tribe of Oklahoma*, 498 U.S. 505 (1991).

C. Taxing Powers of Indian Tribes

Indian tribes have an inherent sovereign power to tax transactions occurring on Indian lands held in trust that significantly involve the Indian tribe or its members.³¹ For transactions occurring on lands not held in trust within an Indian reservation, an Indian tribe generally may tax its members, but may not tax non-members unless it has civil authority over the non-members.³² Without an express grant of civil authority by Congress, an Indian tribe may only exercise civil authority over non-members in two cases: (1) if non-members have entered consensual relationships with the Indian tribe or tribal members, and (2) if the conduct of non-members threatens or has some direct effect on the political integrity, economic security, or the health and welfare of the Indian tribe.³³ A non-member's conduct of a business on land owned in fee within a reservation is not itself a sufficient basis for the exercise of civil authority by an Indian tribe.³⁴

³¹ *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130 (1982).

³² *Montana v. United States*, 450 U.S. 544 (1981).

³³ *Ibid.*

³⁴ *Atkinson Trading Co. v. Shirley*, 532 U.S. 645 (2001) (tribe held not to have authority to apply a hotel occupancy tax on a hotel owned by non-members on land held in fee located within a reservation).

D. Alaska Native Settlement Trusts

The Alaska Native Claims Settlement Act (“ANCSA”)³⁵ established Alaska Native Corporations to hold property for Alaska Natives. Alaska Natives are generally the only permitted common shareholders of those corporations under section 7(h) of ANCSA, unless an Alaska Native Corporation specifically allows other shareholders under specified procedures.

ANCSA permits an Alaska Native Corporation to transfer money or other property to an Alaska Native Settlement Trust (“Settlement Trust”) for the benefit of beneficiaries who constitute all or a class of the shareholders of the Alaska Native Corporation, to promote the health, education and welfare of beneficiaries and to preserve the heritage and culture of Alaska Natives.³⁶

Alaska Native Corporations and Settlement Trusts, as well as their shareholders and beneficiaries, are generally subject to tax under the same rules and in the same manner as other taxpayers that are corporations, trusts, shareholders, or beneficiaries.

Special tax rules enacted in 2001 allow an election to use a more favorable tax regime for transfers of property by an Alaska Native Corporation to a Settlement Trust and for income taxation of the Settlement Trust. There is also simplified reporting to beneficiaries. These rules are currently scheduled to expire for taxable years beginning after December 31, 2012.³⁷

Under the special tax rules, a Settlement Trust may make an irrevocable election to pay tax on taxable income at the lowest rate specified for individuals, (rather than the highest rate that is generally applicable to trusts) and to pay tax on capital gains at a rate consistent with being subject to such lowest rate of tax. As described further below, beneficiaries may generally thereafter exclude from gross income distributions from a trust that has made this election. Also, contributions from an Alaska Native Corporation to an electing Settlement Trust generally will not result in the recognition of gross income by beneficiaries on account of the contribution. An electing Settlement Trust remains subject to generally applicable requirements for classification and taxation as a trust.

A Settlement Trust distribution is excludable from the gross income of beneficiaries to the extent of the taxable income of the Settlement Trust for the taxable year and all prior taxable years for which an election was in effect, decreased by income tax paid by the Trust, plus tax-exempt interest from State and local bonds for the same period. Amounts distributed in excess of the amount excludable is taxed to the beneficiaries as if distributed by the sponsoring Alaska

³⁵ 43 U.S.C. 1601 *et. seq.*

³⁶ With certain exceptions, once an Alaska Native Corporation has made a conveyance to a Settlement Trust, the assets conveyed shall not be subject to attachment, distraint, or sale or execution of judgment, except with respect to the lawful debts and obligations of the Settlement Trust.

³⁷ These rules were enacted by the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, sec. 671, and were originally scheduled to expire for taxable years beginning after December 31, 2010. See H.R. Rep. No. 107-84 (2001). In 2010, the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, sec. 101(a), extended the rules through taxable years beginning on or before December 31, 2012.

Native Corporation in the year of distribution by the Trust, which means that the beneficiaries must include in gross income as dividends the amount of the distribution, up to the current and accumulated earnings and profits of the Alaska Native Corporation. Amounts distributed in excess of the current and accumulated earnings and profits are not included in gross income by the beneficiaries.

A special loss disallowance rule reduces (but not below zero) any loss that would otherwise be recognized upon disposition of stock of a sponsoring Alaska Native Corporation by a proportion, determined on a per share basis, of all contributions to all electing Settlement Trusts by the sponsoring Alaska Native Corporation. This rule prevents a stockholder from being able to take advantage of a decrease in value of an Alaska Native Corporation that is caused by a transfer of assets from the Alaska Native Corporation to a Settlement Trust.

The fiduciary of an electing Settlement Trust would be obligated to provide certain information relating to distributions from the trust in lieu of reporting requirements under Section 6034A.

The election to pay tax at the lowest rate is not available in certain disqualifying cases where transfer restrictions have been modified to allow a transfer of either: (a) a beneficial interest that would not be permitted by section 7(h) of the Alaska Native Claims Settlement Act if the interest were Settlement common stock, or (b) any stock in an Alaska Native Corporation that would not be permitted by section 7(h) if it were Settlement common stock and the Alaska Native Corporation thereafter makes a transfer to the Trust. Where an election is already in effect at the time of such disqualifying transfers, the special rules applicable to an electing trust cease to apply and rules generally applicable to trusts apply. In addition, the distributable net income of the trust is increased by undistributed current and accumulated earnings and profits of the trust, limited by the fair market value of trust assets at the date the trust becomes so disposable. The effect is to cause the trust to be taxed at regular trust rates on the amount of recomputed distributable net income not distributed to beneficiaries, and to cause the beneficiaries to be taxed on the amount of any distributions received consistent with the applicable tax rate bracket.

II. SELECTED FEDERAL TAX RULES AND ISSUES RELATING TO INDIAN TRIBES AND THEIR MEMBERS

A. The General Welfare Doctrine

Present Law

Except as otherwise provided by law, gross income means all income from whatever source derived.³⁸ The general welfare doctrine is an IRS administrative rule that operates to exclude certain payments from gross income. Excludable payments generally consist of payments: (1) made from a governmental fund, (2) for the promotion of general welfare (on the basis of the need of the recipient),³⁹ and (3) which do not represent compensation for services. Examples of excludable benefits include disaster relief,⁴⁰ adoption assistance,⁴¹ housing and utility subsidies for low income persons,⁴² and government benefits paid to the blind.⁴³

Issues Relating to Application of General Welfare Doctrine to Indian Tribes and Their Members

There is some uncertainty concerning the application of the general welfare doctrine to certain benefits provided by Indian tribes to their members. Benefits that have been scrutinized by the IRS include payments for housing, cultural, education, and elder programs provided by

³⁸ Sec. 61(a).

³⁹ Guidance as to whether the need of the recipient (taken into account under the second requirement of the general welfare exclusion) must be based solely on financial means or whether the need can be based on a variety of other considerations including health, educational background, or employment status, has been mixed. Private Letter Ruling 199924026, March 19, 1999 (nonreimbursable economic development grants made by a tribal government to eligible members were held to be excludable from income); Chief Counsel Advice 200021036, May 25, 2000 (excluding state adoption assistant payments made to individuals adopting special needs children without regard to financial means of parents; the children were considered to be the recipients); Private Letter Ruling 200409033, November 24, 2003 (education assistance payments made to qualifying Indian tribe members with an income below the national median income level were not includible in income while payments made to those with income above the national median were includible in income); Private Letter Ruling 200632005, April 13, 2006 (excluding payments made by Indian tribe to members based on multiple factors of need pursuant to housing assistance program); Chief Counsel Advice 200648027, July 25, 2006 (excluding subsidy payments based on financial need of recipient made by state to certain participants in state health insurance program to reduce cost of health insurance premiums).

⁴⁰ Rev. Rul. 76-144, 1976-1 C.B. 17.

⁴¹ Rev. Rul. 74-153, 1974-1 C.B. 20.

⁴² Rev. Rul. 78-170, 1978-1 C.B. 24; Rev. Rul. 76-395, 1976-2 C.B. 16; *Graff v. Commissioner*, 74 TC 743, 753-754 (1980) (court acknowledged that rental subsidies under Housing Act were excludable under general welfare doctrine but found that payments at issue made by HUD on taxpayer landlord's behalf were taxable income to him), *aff'd. per curiam* 673 F.2d 784 (5th Cir. 1982).

⁴³ Rev. Rul. 57-102, 1957-1 C.B. 26

tribal governments.⁴⁴ The issue is whether the tribal governments can provide such benefits without considering the financial need of the members.

Recently, the IRS has solicited comments from Indian tribes concerning the application of the general welfare doctrine.⁴⁵ Proponents have argued that such benefits should be excluded under the doctrine because they are addressing a social welfare need.⁴⁶ Others have suggested that the doctrine should apply to these benefits only where they are available based on financial need and not tribal status.⁴⁷

⁴⁴ Prior to the enactment of the Patient Protection and Affordable Care Act, Pub. L. No. 111-148, March 23, 2010, health care benefits provided to Indian tribe members would also have been on this list. Section 9021 of that Act added section 139D to the Code, which specifically excludes qualified Indian health care benefits from income.

⁴⁵ Notice 2011-94, 2011-49 I.R.B. 834, December 5, 2011.

⁴⁶ In response to Notice 2011-94, the National Congress of American Indians, the Native American Finance Officers Association, the United South and Eastern Tribes, Inc., the Affiliated Tribes of Northwest Indians, and the California Association of Tribal Governments, have asked the Treasury Department and the IRS to consider guidance reaffirming that the general welfare doctrine may be satisfied by government programs designed to address a social welfare need, including health care, housing, and educational needs, as well as social needs related to tribal language and culture, instead of limiting the doctrine to government programs that require individualized determinations of financial need. Available at http://www.usetinc.org/Libraries/meeting_page_documents/Joint_Taskforce_GW_Comments_-_Final.sflb.ashx.

⁴⁷ See Testimony of Sarah Hall Ingram, Commissioner, Tax Exempt and Government Entities, Internal Revenue Service, before the Senate Committee on Indian Affairs, "Oversight Hearing to Examine the Federal Tax Treatment of Health Care Benefits Provided by Tribal Governments to Their Citizens," September 17, 2009, available at <http://www.indian.senate.gov/hearings/hearing.cfm?hearingID=e655f9e2809e5476862f735da14f93c1>. In her testimony, Ms. Ingram expressed the view that the general welfare exclusion does not apply to persons with significant income or assets, and that any such extension would represent a departure from well established administrative practice. She further opined that application of the general welfare exclusion to an Indian tribal government providing coverage or benefits to tribal members is dependent upon the structure and administration of the particular program.

B. Indian Tribal Governments Treated as States for Certain Purposes (sec. 7871)

Present Law

1. In general

Section 7871 expressly provides that Indian tribal governments are treated as States for certain tax purposes.⁴⁸ First, tribal governments may be recipients of deductible charitable contributions for income, estate, and gift tax purposes. Second, tribal governments are extended the treatment provided to States under the following excise taxes: tax on special fuels, manufacturers excise taxes, communications excise tax, and tax on use of certain highway vehicles. Special treatment relating to excise taxes is available to tribal governments only with regard to transactions involving the exercise of an essential governmental function, as described below,⁴⁹ by the Indian tribal government. Third, taxes paid to Indian tribal governments are deductible for income tax purposes to the same extent as State taxes. Fourth, Indian tribal governments may issue tax-exempt bonds under certain conditions described further below.⁵⁰

In addition, Indian tribal governments are treated as States for purposes of: (1) unrelated business income tax rules that apply to State colleges and universities, (2) treatment of amounts received under a disability and sickness fund maintained by a State, (3) the rules relating to tax-sheltered annuities,⁵¹ (4) obligations issued on discount bonds, (5) the tax on excess expenditures to influence legislation, and (6) private foundation rules.

2. Tax-exempt bonds

In general

Tribal governments may issue tax-exempt bonds⁵² in several types of circumstances if they meet requirements applicable to bonds issued by States and local governments and certain

⁴⁸ This provision was enacted by the Indian Tribal Government Tax Status Act of 1982, Pub. L. No. 97-473, sec. 202(a) (January 4, 1983), *as amended by* the Deficit Reduction Act of 1984, Pub. L. No. 98-369, sec. 1065(a) (August 18, 1984), and the Omnibus Reconciliation Act of 1987, Pub. L. No. 100-203 (December 22, 1987).

⁴⁹ Section 7871(e) limits the term essential governmental function to exclude any function that is not customarily performed by State and local governments with general taxing powers. This provision was added by the Omnibus Budget Reconciliation Act of 1987, Pub. L. No. 100-203, sec. 10632(a) (December 22, 1987).

⁵⁰ For more detailed information regarding the rules applicable to tax-exempt bonds, see Joint Committee on Taxation, *Present Law and Background Information Related to State and Local Government Finance* (JCX-36-12), April 23, 2012.

⁵¹ Sec. 403(b). Under Code section 414(d) and section 3(32) of the Employee Retirement Income Security Act of 1974 (“ERISA”), a qualified retirement plan of an Indian tribal government is a governmental plan (and thus exempt from ERISA and various Code requirements) if all of the participants are employees substantially all of whose services are in the performance of essential government functions, but not in the performance of commercial activities (whether or not an essential government function).

⁵² Generally, gross income does not include interest on State or local bonds. Sec. 103.

other rules applicable only to Indian tribes. Indian tribes may issue tax-exempt bonds for governmental purposes, subject to the requirement that substantially all of the proceeds of the issue are used in an essential governmental function, as discussed below. Indian tribes also may issue private activity bonds but only for the purpose of financing manufacturing facilities.⁵³

The Code provides that Indian tribes may also issue a third type of tax-exempt bond called “Tribal economic development bonds” to finance projects and facilities (but not certain gambling facilities casinos) if the bonds would be tax-exempt if issued by a State or local government.⁵⁴ The restriction of essential government function and the limitation on private activity bonds to certain manufacturing facilities do not apply. However, this Code provision is subject to an allocation limit of \$2 billion.

Governmental bond

Like States and local governments, Indian tribes may issue so-called “governmental bonds.” These bonds are bonds the proceeds of which are primarily used to finance governmental facilities or which are repaid with governmental funds. The Code does not expressly define governmental bonds. Instead, bonds are generally treated as governmental bonds if they limit private involvement sufficiently to avoid classification as private activity bonds,⁵⁵ contain arbitrage restrictions,⁵⁶ and satisfy bond registration and information reporting requirements and various other Code restrictions.⁵⁷

Indian tribes must also meet an additional requirement to issue governmental bonds. Specifically, all of the bond proceeds must be used in an essential governmental function⁵⁸ and such function must be customarily performed by State and local governments with general taxing powers.⁵⁹

⁵³ Secs. 7871(c)(3), 103.

⁵⁴ The American Recovery and Reinvestment Act of 2009 (“ARRA”), Pub. L. No. 111-5, sec. 1402, added section 7871(f) to the Code.

⁵⁵ The exclusion from income of interest on State and local bonds does not apply to private activity bonds, unless the bonds are issued for certain permitted purposes (“qualified private activity bonds”) and other Code requirements are met. Secs. 103, 141.

⁵⁶ Secs. 103(b), 148.

⁵⁷ Secs. 103(b), 149.

⁵⁸ Sec. 7871(c).

⁵⁹ Sec. 7871(e). This provision was added by the Omnibus Budget Reconciliation Act of 1987, Pub. L. No. 100-203, sec. 10632(a) (December 22, 1987). Prior to the enactment of this provision, the IRS interpreted the term essential governmental function to include any project for which Federal assistance to Indian tribes may be provided, including some commercial and industrial activities not generally conducted by States and local governments with general taxing powers. See H.R. Conf. Rep. No. 100-495 (1987).

Private Activity Bonds for Tribal Manufacturing Facilities

As with governmental bonds, Indian Tribes are more restricted than States and local governments in their ability to issue private activity bonds. Section 7871(c)(3) permits tribal governments to issue private activity bonds⁶⁰ so long as the bond proceeds are used for manufacturing facilities⁶¹ that are owned and operated by the tribal government on “qualified Indian lands,”⁶² and that employ tribal members.⁶³

A project financed by manufacturing facility bonds must meet requirements as to use, location and ownership, and employment. The use requirement provides that at least 95 percent of the net proceeds of the issue are to be used for the acquisition, construction, or improvement of property that is part of a manufacturing facility and subject to an allowance for depreciation. The location and ownership requirement provides that at least 95 percent of the net proceeds are to be used to finance property to be located on qualified Indian lands of the issuer, which is to be owned and operated by the issuer.⁶⁴ The employment requirement provides that at time of issuance, it is reasonably expected that the aggregate face amount of private activity bonds financing a facility will not exceed 20 times the aggregate wages paid during a future calendar year. The employment requirement must be met each year beginning more than two years after the date of issuance. If the employment requirement is not met for any year for which it applies with respect to an issuance, all bonds that are part of that issuance cease to be tax-exempt to their holders. The annual tribal employment test is in lieu of an annual aggregate volume limit.⁶⁵

⁶⁰ Outside the context of Indian country, private activity bonds are generally bonds in which the State or local government serves as a conduit providing financing to nongovernmental persons. For these purposes, the term “nongovernmental person” includes the Federal government and all other individuals and entities other than States or local governments. Interest on private activity bonds is taxable, unless the bonds are issued for certain purposes permitted by the Code and other requirements are met. Section 7871(c)(3)(C) provides that an obligation to which this paragraph (dealing with the exception for certain private activity bonds used for certain tribal manufacturing facilities) applies shall be treated as a private activity bond.

⁶¹ The term “manufacturing facility” is defined by cross reference to section 144(a)(12)(C) as any facility which is used in the manufacturing or production of tangible personal property (including the processing resulting in a change in the condition of such property).

⁶² “Qualified Indian lands” means land which is held in trust by the United States for the benefit of an Indian tribe. The term “Indian tribe” means any Indian tribe, band, nation, or other organized group or community which is recognized as eligible for the special programs and services provided by the United States to Indians because of their status as Indians. Sec. 7871(c)(3)(E).

⁶³ The Omnibus Budget Reconciliation Act of 1987, P. L. No. 100-203, sec. 10632(b).

⁶⁴ Tribes may jointly finance a manufacturing facility, and the employment test may be met in such case by pro rata apportionment of wages by tribe according to the relative participation of each tribe.

⁶⁵ Manufacturing facility private activity bonds issued by tribes are not subject to State volume caps. See H.R. Conf. Rep. No. 100-495 (1987). Thus, the private activity bonds issued by tribes do not count against the volume cap of the State where the reservation is located. However, persons living on Indian reservations within a State are counted for purposes of calculating that State’s volume cap, thus, States could issue bonds for the benefit of tribal reservations located within the State.

Tribal Economic Development Bonds

Under a provision added to the Code in 2009, Indian tribal governments are permitted to issue “tribal economic development bonds.”⁶⁶ A tribal economic development bond is any bond issued by an Indian tribal government (1) the interest on which would be tax-exempt if issued by a State or local government, and (2) that is designated by the Indian tribal government as a tribal economic development bond.⁶⁷

As a result of this provision, Indian tribes have the authority to issue bonds to finance projects and facilities owned by Indian tribes, located on Indian reservations, but outside the scope of “essential governmental function” bonds, such as convention centers, golf courses, hotels, restaurants, certain entertainment facilities, etc. In addition, Indian tribes have the authority to issue private activity bonds for any one of the seven types of “qualified bonds” used for purposes that Congress has permitted⁶⁸ and are not limited to financing tribal manufacturing facilities. The six other types of qualified private activity bonds include (1) exempt facility bonds;⁶⁹ (2) qualified mortgage bonds⁷⁰ to finance the purchase or repair or rehabilitation of owner-occupied single-family homes located in the jurisdiction of the issuer; (3) qualified veteran’s mortgage bonds⁷¹ to finance veterans’ purchases of owner-occupied single-family homes (as long as a State issued such bonds before June 22, 1984); (4) qualified student loan bonds;⁷² (5) qualified redevelopment bonds⁷³ to finance the redevelopment of blighted areas; and (6) qualified 501(c)(3) bonds⁷⁴ to fund the exempt activities of a 501(c)(3) organization.

⁶⁶ ARRA, Pub. L. No. 111-5, sec. 1402 added sec. 7871(f) to the Code.

⁶⁷ Sec. 7871(f)(3). Tribal economic development bonds issued by an Indian tribal government are treated as if such bond were issued by a State except that section 146 (relating to State volume limitations) does not apply. Sec. 7871(f)(2).

⁶⁸ Sec. 141(e) (provides the list of seven qualified private activity bonds). For purposes of section 141, use of bond proceeds by an Indian tribe, or instrumentality thereof, is treated as use by a State.

⁶⁹ Sec. 142. Business facilities eligible for this financing include transportation (airports, ports, local mass commuting, high-speed intercity rail facilities, and qualified highway or surface freight transfer facilities); privately owned and/or operated public works facilities (sewage, solid waste disposal, water, local district heating or cooling, and hazardous waste disposal facilities); privately-owned and/or operated residential rental housing; and certain private facilities for the local furnishing of electricity or gas. Bonds issued to finance “environmental enhancements of hydro-electric generating facilities,” qualified public educational facilities, and qualified green building and sustainable design projects also may qualify as exempt facility bonds.

⁷⁰ Sec. 143.

⁷¹ Sec. 143. Sec. 142(l)(2).

⁷² Sec. 144(b).

⁷³ Sec. 144(c).

⁷⁴ Sec. 145.

The aggregate face amount of bonds that may be designated by any Indian tribal government cannot exceed the amount of national tribal economic development bond limitation allocated to such government.⁷⁵ There is a national bond limitation of \$2 billion, allocated as the Secretary determines appropriate, in consultation with the Secretary of the Interior.⁷⁶

Tribal economic development bonds cannot be used to finance any portion of a building in which class II or class III gaming (as defined in section 4 of the Indian Gaming Regulatory Act) is conducted, or housed, or any other property used in the conduct of such gaming. Nor can tribal economic development bonds be used to finance any facility located outside of the Indian reservation.⁷⁷

Issues Relating to the Issuance of Tax-Exempt Bonds by Indian Tribal Governments

The power of States to issue tax-exempt bonds is not conditioned upon the exercise of an essential governmental function. The existence of an essential governmental function requirement, reflects Congress's concern that the Federal subsidy resulting for tax-exempt bonds be used for governmental activities rather than quasi-commercial or commercial activities that would be carried on by a private business.

Although not defined in the Code, an essential governmental function includes providing for schools, streets, and sewers.⁷⁸ The standard permits financing for facilities comparable to

⁷⁵ Sec. 7871(f)(3)(C).

⁷⁶ Sec. 7871(f)(1)(B). Announcement 2011-71, 2011-46 I.R.B. 770, November 14, 2011 (IRS sought comment from Indian tribal governments on the reallocation of available amounts of national bond volume limitation authority that were previously allocated and have been, or subsequently are, forfeited under Notice 2009-51, 2009-28 I.R.B. 128, July 13, 2009, and Announcement 2010-88, 2010-47 I.R.B. 753, November 22, 2010. According to the Treasury Department, issuance of these bonds through November 2011 has been very limited, comprising less than three percent of the total \$2 billion bond authorization. The Treasury Department believes that the reasons for this lack of actual usage relate mainly to credit challenges facing Indian tribal governments. Department of Treasury, *Report and Recommendations to Congress regarding Tribal Economic Development Bond provision under Section 7871 of the Internal Revenue Code*, December 2011, p. 4, available at <http://www.treasury.gov/resource-center/economic-policy/tribal-policy/Documents/Report%20to%20Congress%20-%20Tribal%20Economic%20Development%20Bonds%20-%20FINAL%2012.19.11.pdf>.

⁷⁷ Sec. 7871(f)(3)(B).

⁷⁸ H. Rep. No. 97-894, 97th Cong. 2d Sess. 16-17 (1982). The phrase “essential governmental function” also appears in another section of the Code dealing with exempting income derived from the exercise of any essential governmental function and accruing to a State or any political subdivision. See sec. 115. The IRS, in various rulings, has interpreted this section to apply to the income of an entity organized separately from a State or its political subdivision. Rev. Rul. 71-131, 1971-1 C.B. 28; Rev. Rul. 77-261, 1977-2 C.B. 45. Rev. Rul. 77-261, 1977-2 C.B. 45 (the income of a fund, established under a written declaration of trust to the pool the temporary investments of the state and its political subdivisions, is excludable from gross income under section 115(1) of the Code. The fund was authorized by state statute, managed by the state treasurer, and benefited only the state and its political subdivisions). Private Letter Ruling 200008024, February 25, 2000 (the income from a corporation managed by government officials which was incorporated by a state authority for various purposes is excludible under section 115 because it performed the same tasks that States and political subdivisions perform. The corporation was formed: (i) to enable governmental entities to pool their purchasing power to take advantage of volume discounts; (ii) to reduce costs by consolidating bidding and contracting procedures; (iii) to serve as a

facilities that are customarily acquired or constructed and operated by States and local governments such as offices for the tribal government and a lodge owned and operated by a tribal government.⁷⁹

An essential governmental function has been interpreted as not including commercial or industrial activities.⁸⁰ For some purposes, commercial activities include hotels, casinos, service stations, convenience stores, and marinas.⁸¹

Opponents of the essential governmental function standard may argue that there is a lack of clarity regarding what types of projects Indian tribes can undertake. On the other hand, the lack of clarity seems to exist only with respect to projects that are not usual performed by States and local governments such as private rental housing, cement factories, or mirror factories.⁸²

products, services, and financing resource for government agencies; and (iv) to assist governmental entities with financing for businesses that contribute to the community. The corporation was precluded from distributing its property or profits to any private person). A private letter ruling binds only the IRS and the taxpayer who requests guidance and therefore, may not be cited or relied upon as precedent. Field Service Advice 200247012, August 12, 2002 (construction and operation of a golf course by an Indian tribe is not an “essential governmental function” because of the commercial nature of the golf course, notwithstanding the fact that its construction and operation are customary government functions).

⁷⁹ H.R. Rep. No. 100-495, p. 1012, n.5 (1987).

⁸⁰ See Advance Notice of Proposed Rulemaking (Definition of Essential Governmental Function Under Section 7871 and Limitation to Activities Customarily Performed by States and Local Governments), 71 Fed. Reg. 45474 (August 9, 2006). The notice provides that “an activity will be considered an essential governmental function that is customarily performed by State and local governments if: (1) There are numerous State and local governments with general taxing powers that have been conducting the activity and financing it with tax-exempt governmental bonds, (2) State and local governments with general taxing powers have been conducting the activity and financing it with tax-exempt governmental bonds for many years, and (3) the activity is not a commercial or industrial activity. The proposed regulations will further provide that examples of activities customarily performed by State and local governments include, but are not limited to, public works projects such as roads, schools, and government buildings.” See also Private Letter Ruling 200911001, March 13, 2009 (IRS applied this three part test to determine that ownership and operation of borrower/political subdivision of Indian tribe’s interest in electric generating facility to provide electrical services to tribe is an essential governmental function; IRS noted that municipalities have long owned, operated and financed municipal power utilities often on a tax-exempt basis and that the project was not distinguishable from public works projects such as roads, school, or governmental buildings which lack a profit-making objective since Tribal law required the borrower to operate on a non-profit basis); Private Letter Ruling 200648024, December 1, 2006 (IRS applied this three part test to determine that construction of a tribal government building to house various administrative offices, emergency services, a cultural center, a museum, as well as infrastructure improvements, are essential governmental functions; IRS concluded that numerous State and local governments have owned and operated museums and financed them with tax-exempt bonds and infrastructure improvements did not become commercial by virtue of benefiting commercial operations).

⁸¹ See generally, Notice 2006-89, 2006-43 I.R.B. 772 (summarizes the changes made to section 414(d) of the Code under which plans established and maintained by Indian tribal governments and certain related entities are governmental plans and provides transition relief with respect to compliance); Notice 2007-67, 2007-35 I.R.B. 467 (extended transitional relief for plans of Indian tribal governments); see also Joint Committee on Taxation, *Technical Explanation of H.R. 4, the “Pension Protection Act of 2006,” as Passed by the House on July 28, 2006, and as Considered by the Senate on August 3, 2006* (JCX-38-06), August 3, 2006.

⁸² See H.R. Rep. No. 100-391, p. 1139 (1987). As discussed above, it is clear that tax-exempt bonds are permitted for Indian tribes that develop schools, roads, sewers, and government offices.

These activities more closely resemble those activities for which private activity bonds are issued, an area in which Congress has expressed concern and provided various rules and limitations for State issuance.⁸³

Tax-exempt private activity bonds that are issued by States and local governments generally are limited in both approved type of facility and in volume. Thus, the States must abide by a volume limitation on the use of the Federal subsidy for private commercial activities. The State volume limits on private activity bonds are based on State population or a minimum floor amount for small States. Tribal economic development bonds, which allow tribes to issue private activity and other bonds on the generally the same basis as States, provide for a national volume limit of \$2 billion.

The Treasury Department recently published a study analyzing the tax treatment of tribal bonds.⁸⁴ The study provided the following four recommendations for tax-exempt bonds issued by Indian tribes: (i) for tax-exempt governmental bonds, Indian tribes should be treated the same as State and local governments and the “essential governmental function” standard should be repealed; (ii) for private activity bonds, Indian tribes should have permanent authorization to issue such bonds for the types of projects and activities that are allowed for State and local governments, subject to an annual national volume cap tailored to the Indian Country (to be allocated amongst the tribal governments by the Department of the Treasury); (iii) allow Indian tribes to use tax-exempt bonds to finance projects that are located on Indian reservations and also for projects that are both (a) contiguous to, within reasonable proximity of, or have a substantial connection to an Indian reservation; and (b) provide goods or services to resident populations of Indian reservations; and (iv) retain restrictions against using tax-exempt financing for certain gaming projects but gaming revenues may continue to be used as a source of payment or security for tax-exempt bonds that finance eligible projects. Some may argue that a volume limitation is appropriate for private activity bonds, however, the allocation of that limited volume by the Department of Treasury may not give tribal governments the flexibility to finance the projects the tribes have determined are best suited for their economic needs.

Neither volume limitations nor the elimination of restrictions on types of issuance addresses the difficulties some tribes have in accessing the bond market due to limited revenue sources and instances of poor credit quality. Although \$2 billion in tribal authority was available, very few bonds were actually issued. Thus some may argue, that assistance in making tribal bonds more attractive to the bond market would be of more assistance to tribes.

⁸³ Sec. 141.

⁸⁴ Section 1402(b) of the American Recovery and Reinvestment Act of 2009, P.L. No. 111-5, directs the Secretary of the Treasury to conduct a study of the effects of this provision and to report to Congress on the results of the study and recommendations. As part of this report, the Treasury Department noted that the total amount of tax-exempt bonds (including tribal economic development bonds) issued by tribal governments during 2009 and 2010 was \$415.52 million. Department of Treasury, Report and Recommendations to Congress regarding Tribal Economic Development Bond provision under Section 7871 of the Internal Revenue Code, December 2011, Appendix A, available at <http://www.treasury.gov/resource-center/economic-policy/tribal-policy/Documents/Report%20to%20Congress%20-%20Tribal%20Economic%20Development%20Bonds%20-%20FINAL%2012.19.11.pdf>.

C. Gaming Activities of Indian Tribes⁸⁵

1. Overview

Gaming activities have become a significant source of revenue for many Indian tribes. Indian gaming is a \$26.5 billion-per-year industry, with 236 Indian tribes operating 422 casinos of varying sizes within 28 of the States.⁸⁶

Such activities generally are regulated under the Indian Gaming Regulatory Act (“IGRA”),⁸⁷ which establishes a detailed regulatory, recordkeeping, and reporting regime for tribal gaming. Under the IGRA, the National Indian Gaming Commission (“NIGC”) has general oversight responsibility for Indian gaming.⁸⁸ Currently, certain forms of online gambling are prohibited by State or Federal law.⁸⁹

The IRS has responsibility for Federal tax issues that relate to Indian gaming. Below is a discussion of several of these Federal tax issues, including: (1) the taxation of income from

⁸⁵ For additional information on Federal tax and regulatory treatment of gaming activities of Indian Tribes and Indian Tribe Members, see Joint Committee on Taxation, *Overview of Federal Tax Laws and Reporting Requirements Relating to Gambling in the United States* (JCX-28-10), May 17, 2010.

⁸⁶ Press Release, National Indian Gaming Commission, “National Indian Gaming Commission Announces 2010 Industry Gross Gaming Revenue,” July 18, 2011, available at http://www.nigc.gov/Media/Press_Releases/2011_Press_Releases/PR-175_07-2011.aspx.

⁸⁷ 25 U.S.C. secs. 2701-2721.

⁸⁸ This responsibility could extend to Tribal internet gambling in the future if any of the Congressional proposals to legalize internet gambling become law.

⁸⁹ Gambling that is prohibited when conducted in person is ordinarily outlawed when conducted online. Some states ban Internet gambling explicitly while others rely upon their generally applicable gambling laws. There are many Federal gambling laws (including at least seven Federal criminal statutes), most enacted to prevent unwelcome intrusions of interstate or international gambling into States where the activity in question has been outlawed. See Charles Doyle, Congressional Research Service, *Internet Gambling: An Overview of Federal Criminal Law* (97-619), January 24, 2012, p.1, available at <http://www.crs.gov/Products/RL/PDF/97-619.pdf>.

Two Federal criminal statutes often mentioned in this context are the Wire Act (18 U.S.C. sec. 1084), which generally outlaws the use of interstate telephone facilities by gambling operators to transmit bets or gambling-related information, and the Unlawful Internet Gambling Enforcement Act (31 U.S.C. sec. 5361 et seq.), which generally makes financial institutions liable for processing certain illegal online gambling transactions. The Wire Act is most often cited as the basis for criminalizing online gambling operations. However, the Wire Act has never been successfully applied to any form of gambling aside from sports betting. For example, the United States Fifth Circuit Court of Appeal has concluded that the Wire Act does not apply to Internet casino gambling that does not involve sports betting. *In Re MasterCard International, Inc., Internet Gambling Litigation*, 132 F. Supp. 2d 468 (E.D. La. 2001), aff’d 313 F.3d 257 (5th Cir. 2002). Along the same lines, the Department of Justice has recently reversed a long-held position by stating that the only online gaming the Wire Act applies to is sports betting. Memorandum Opinion for the Assistant Attorney General, Criminal Division, from Virginia A. Seitz, Assistant Attorney General, Office of Legal Counsel, “Whether Proposals by Illinois and New York to Use the Internet and Out-of-State Transaction Processors to sell Lottery Tickets to in-State Adults Violate the Wire Act, September 20, 2011.

gaming operations; (2) the tax treatment of gambling winnings and losses, including withholding and reporting requirements; and (3) excise taxes on wagering activities.

2. Federal tax treatment of income from gaming operations

As is discussed above, Indian tribes and wholly owned tribal corporations chartered under Federal law generally are not subject to income tax. Therefore, gaming income of such Indian tribes or tribal corporations generally is not taxable. A tribal corporation incorporated under State law may, however, be subject to tax on such income.

Under certain circumstances, the IGRA permits Indian tribes to make per capita distributions to members from revenue derived from certain gaming activities conducted or licensed by the Indian tribe. The IGRA explicitly subjects the receipt of such distributions to Federal income tax.⁹⁰ Such distributions also are subject to special withholding requirements.⁹¹

3. Treatment of gambling winnings and losses

Gains from wagering transactions are includible in a taxpayer's gross income. A taxpayer who itemizes deductions may deduct losses from wagering transactions, but only to the extent the taxpayer recognizes gains from such transactions on the taxpayer's income tax return.⁹²

Withholding requirements

The IGRA provides that Code provisions concerning the reporting and withholding of taxes with respect to gambling operations shall apply to Indian tribes in the same way as they apply to States.⁹³ In general, proceeds from a wagering transaction are subject to withholding at a rate of 25 percent if the proceeds exceed \$5,000 and are at least 300 times as large as the amount wagered.⁹⁴ In the case of sweepstakes, wagering pools, or lotteries, proceeds from a wager are subject to withholding at a rate of 25 percent if the proceeds exceed \$5,000, regardless

⁹⁰ 25 U.S.C. sec. 2710(b)(3)(D), Pub. L. No. 100-497 (October 17, 1988).

⁹¹ Sec. 3402(r).

⁹² Sec. 165(d).

⁹³ 25 U.S.C. sec. 2719(d) ("The provisions of the Internal Revenue Code of 1986 (including sections 1441, 3402(q), 6041, and 6050I, and chapter 35 of such Code [26 USCS §§ 1441, 3402(q), 6041, and 6050I, and 4401 et seq.]) concerning the reporting and withholding of taxes with respect to the winnings from gaming or wagering operations shall apply to Indian gaming operations conducted pursuant to this Act...in the same manner as such provisions apply to State gaming and wagering operations").

⁹⁴ Sec. 3402(q)(3)(A).

of the odds of the wager.⁹⁵ In general, no withholding tax is imposed on winnings from bingo, keno, or slot machines.⁹⁶

For withholding purposes, the proceeds from a wagering transaction are determined by subtracting the amount wagered from the amount received. Any non-monetary proceeds that are received are taken into account at fair market value.⁹⁷ Amounts paid with respect to identical wagers are treated as paid with respect to a single wager.⁹⁸

Information reporting requirements

Present law imposes information reporting requirements that enable the IRS to verify the correctness of taxpayers' returns. In general, every person engaged in a trade or business is required to file information returns for each calendar year for payments of \$600 or more made in the course of the payor's trade or business. Regulations provide generally that a gambling winning is reportable on Form W-2G only if the amount paid with respect to the wager is \$600 or more and the proceeds are at least 300 times the amount of the wager.⁹⁹

Regulations describe special information reporting rules that apply for purposes of winnings from bingo, keno, and slot machines. Specifically, regulations provide that winnings (not reduced by the wager) of \$1,200 or more from bingo or slot machines, and winnings (reduced by the wager) of \$1,500 or more from keno, are subject to information reporting on Form W-2G, regardless of the odds of the wager.¹⁰⁰

4. Wagering excise and occupational taxes

Although Federally recognized Indian tribes and wholly owned tribal corporations chartered under Federal law are exempt from income taxation, they are subject to Federal excise taxes on wagering. The wagering excise taxes are not included in the list¹⁰¹ of excise taxes for which tribal governments are treated as States and the Supreme Court has ruled that Indian tribes are subject to these taxes even though States are exempt.¹⁰²

⁹⁵ Sec. 3402(q)(3)(B) and (C).

⁹⁶ Sec. 3402(q)(5). Gambling winnings, including winnings from bingo, keno, and slot machines, are subject to backup withholding under certain circumstances. Sec. 3406.

⁹⁷ Sec. 3402(q)(4).

⁹⁸ Treas. Reg. sec. 31.3402(q)-1(c)(1)(ii).

⁹⁹ Treas. Reg. sec. 31.3406(g)-2(d)(3).

¹⁰⁰ Treas. Reg. sec. 7.6041-1.

¹⁰¹ Sec. 7871(a)(2).

¹⁰² *Chickasaw Nation v. United States*, 534 U.S. 84 (2001) (holding that the Indian Gambling Regulatory Act does not exempt tribal governments from Federal excise taxes on wagering in the same manner as States).

Two excise taxes generally apply to wagering activities of gaming establishments owned by Indian tribes (and non-Indians): a wagering tax and an occupational tax. The Code imposes a tax of 0.25 percent on any wager authorized under the law of the State in which the wager is accepted (the rate increases to 2.0 percent of any wager that is not so authorized).¹⁰³ Each person who is engaged in the business of accepting wagers is liable for the tax on all wagers placed with such person. Each person who conducts any wagering pool or lottery is liable for the tax on all wagers placed in such pool or lottery. Certain wagering activities conducted by States (sweepstakes, wagering pools, or lotteries) are exempt from these excise taxes.¹⁰⁴ Wagers placed in a coin-operated device, such as a slot machine, and certain wagers placed with State-licensed parimutual wagering enterprises also are exempt from the wagering tax.¹⁰⁵ Native American tribal governments are not treated as States for purposes of the wagering tax and related occupational tax.¹⁰⁶

The Code also imposes an occupational tax of \$50 per year (\$500 in the case of persons accepting wagers not authorized by the law of the State in which the wager is accepted) for each person liable for the wagering tax and for each person who is engaged in receiving wagers for or on behalf of a person liable to pay the wagering tax.¹⁰⁷ In general, where multiple persons do business in co-partnership at any one place, only one occupational tax must be paid.¹⁰⁸

In some cases, Indian tribes and other entities may accept wagers that are not authorized under the law of the State in which the wagers are accepted. In these cases, the higher 2.0 percent excise tax on wagers and \$500 occupational tax apply.

Each person required to pay the occupational tax must register with the IRS. The registration must include: (1) the person's name and place of residence; (2) if such person is liable for the wagering excise tax, each place of business where the activity which makes him so liable is carried on, and the name and place of residence of each person who accepts wagers for such person or on his behalf; and (3) if he is engaged in accepting wagers for or on behalf of any person liable for the wagering excise tax, the name and place of residency of each such person.¹⁰⁹ The Code authorizes the Secretary to prescribe, by regulation, such supplemental information from persons required to register as may be needed to enforce the wagering provisions ("supplemental registration").¹¹⁰ Pursuant to Treasury regulations, a supplemental registration

¹⁰³ Sec. 4401.

¹⁰⁴ Sec. 4402(3).

¹⁰⁵ Sec. 4402(1) and (2).

¹⁰⁶ *Chickasaw Nation v. United States*, 534 U.S. 84 (2001) (holding that the Indian Gambling Regulatory Act does not exempt tribal governments from gambling related taxes in the same manner as States).

¹⁰⁷ Sec. 4411.

¹⁰⁸ Sec. 4902.

¹⁰⁹ Sec. 4412.

¹¹⁰ Sec. 4412(c), Treas. Reg. sec. 44.4412-1(b)(2) and (b)(3); and Treas. Reg. secs. 44.4905-1 (relating to change of ownership) and 44.4905-2 (relating to change of address).

must be filed if one of the following occurs: (1) the taxpayer changes either the business or home address; (2) the business of a deceased person who had paid the occupational tax is continued by the surviving spouse or child, executor, administrator, or other legal representative; (3) the business is continued by a receiver or trustee in bankruptcy; (4) the business is continued by an assignee for creditors; (5) one or more members withdraws from the firm or partnership; or (6) the corporate name is changed. A supplemental registration also must be filed each time an additional employee or agent is engaged to receive wagers.

In the event of a failure to register by a person required to pay the occupational tax, the Code imposes a penalty of \$50.¹¹¹ Any person who is liable for the occupational tax but does not pay such tax shall, in addition to being liable for such tax, be fined not less than \$1,000 and not more than \$5,000.¹¹²

¹¹¹ Sec. 7272(a).

¹¹² Sec. 7262.

D. Economic Development Incentives

The Code has several provisions relating to fostering economic development in Indian country. Except for a provision relating to Indian coal, all are currently expired.

1. Accelerated depreciation for business property on Indian reservations (sec. 168)

With respect to certain property used in connection with the conduct of a trade or business within an Indian reservation and placed in service prior to January 1, 2012, depreciation deductions under section 168(j)¹¹³ are determined using the following recovery periods:

Table 1.—Comparison of Applicable Recovery Periods

MACRS	Indian Reservation Property
3-year property	2 years
5-year property	3 years
7-year property	4 years
10-year property	6 years
15-year property	9 years
20-year property	12 years
Residential real property (27.5 years)	27.5 years (same)
Nonresidential real property (39 years)	22 years

“Qualified Indian reservation property” eligible for accelerated depreciation includes property described in the table above which is: (1) used by the taxpayer predominantly in the active conduct of a trade or business within an Indian reservation; (2) not used or located outside the reservation on a regular basis; (3) not acquired (directly or indirectly) by the taxpayer from a person who is related to the taxpayer;¹¹⁴ and (4) not property placed in service for purposes of conducting gaming activities.¹¹⁵ Certain “qualified infrastructure property” may be eligible for the accelerated depreciation even if located outside an Indian reservation, provided that the

¹¹³ This provision was enacted by the Omnibus Reconciliation Act of 1993, Pub. L. No. 103-66, sec. 13321(a). The provision originally applied to property placed in service on or after January 1, 1994 and before January 1, 2004, but was extended to 2005, 2006, 2008, 2010, and 2012 as follows: Pub. L. No. 107-147, sec. 613(b); Pub. L. No. 108-311, sec. 316; Pub. L. No. 109-432, Division A, sec. 112(a); Pub. L. No. 110-343, Division C, sec. 315(a); and Pub. L. No. 111-312, sec. 739(a). The Taxpayer Relief Act of 1997, Pub. L. No. 105-34, sec. 1604(c)(2), clarified the definition of “Indian reservation” as pertaining to the State of Oklahoma, effective as if included in the Omnibus Reconciliation Act of 1993.

¹¹⁴ For these purposes, related persons is defined in section 465(b)(3)(C).

¹¹⁵ Sec. 168(j)(4)(A).

purpose of such property is to connect with qualified infrastructure property located within the reservation (e.g., roads, power lines, water systems, railroad spurs, and communications facilities).¹¹⁶

An “Indian reservation” means a reservation as defined in section 3(d) of the Indian Financing Act of 1974 or section 4(10) of the Indian Child Welfare Act of 1978.¹¹⁷ For purposes of the preceding sentence, section 3(d) is applied by treating “former Indian reservations in Oklahoma” as including only lands that are (1) within the jurisdictional area of an Oklahoma Indian tribe as determined by the Secretary of the Interior, and (2) recognized by such Secretary as an area eligible for trust land status under 25 C.F.R. Part 151 (as in effect on August 5, 1997).

The depreciation deduction allowed for regular tax purposes is also allowed for purposes of the alternative minimum tax.

2. Indian employment tax credit (sec. 45A)

In general, for taxable years beginning before January 1, 2012, a credit against income tax liability is allowed to employers for the first \$20,000 of qualified wages and qualified employee health insurance costs paid or incurred by the employer with respect to certain employees.¹¹⁸ The credit is equal to 20 percent of the excess of eligible employee qualified wages and health insurance costs during the current year over the amount of such wages and costs incurred by the employer during 1993. The credit is an incremental credit, such that an employer’s current-year qualified wages and qualified employee health insurance costs (up to \$20,000 per employee) are eligible for the credit only to the extent that the sum of such costs exceeds the sum of comparable costs paid during 1993. No deduction is allowed for the portion of the wages equal to the amount of the credit.

Qualified wages means wages paid or incurred by an employer for services performed by a qualified employee.¹¹⁹ A qualified employee means any employee who is an enrolled member of an Indian tribe or the spouse of an enrolled member of an Indian tribe, who performs substantially all of the services within an Indian reservation, and whose principal place of abode while performing such services is on or near the reservation in which the services are performed.¹²⁰ An “Indian reservation” is a reservation as defined in section 3(d) of the Indian Financing Act of 1974 or section 4(1) of the Indian Child Welfare Act of 1978.¹²¹ For purposes

¹¹⁶ Sec. 168(j)(4)(C).

¹¹⁷ Sec. 168(j)(6).

¹¹⁸ This section was enacted by the Omnibus Reconciliation Act 1993, Pub. L. No. 103-66, sec. 13322(b). The provision originally applied to wages paid or incurred on or after January 1, 1994 and before January 1, 2004, but was extended to 2005, 2006, 2008, 2010, and 2012 as follows: Pub. L. No. 107-147, sec. 613(a); Pub. L. No. 108-311, sec. 315; Pub. L. No. 109-432, Division A, sec. 111(a); Pub. L. No. 110-343, Division C, sec. 314(a); and Pub. L. No. 111-312, sec. 732(a).

¹¹⁹ Sec. 45A(b)(1).

¹²⁰ Sec. 45(c)(1).

¹²¹ Sec. 45A(c)(7). See sec. 168(j)(6).

of the preceding sentence, section 3(d) is applied by treating “former Indian reservations in Oklahoma” as including only lands that are (1) within the jurisdictional area of an Oklahoma Indian tribe as determined by the Secretary of the Interior, and (2) recognized by such Secretary as an area eligible for trust land status under 25 C.F.R. Part 151 (as in effect on August 5, 1997).

An employee is not treated as a qualified employee for any taxable year of the employer if the total amount of wages paid or incurred by the employer with respect to such employee during the taxable year exceeds an amount determined at an annual rate of \$30,000 (which after adjustment for inflation is currently \$45,000).¹²² In addition, an employee will not be treated as a qualified employee under certain specific circumstances, such as where the employee is related to the employer (in the case of an individual employer) or to one of the employer’s shareholders, partners, or grantors.¹²³ Similarly, an employee will not be treated as a qualified employee where the employee has more than a five percent ownership interest in the employer. Finally, an employee will not be considered a qualified employee to the extent the employee’s services relate to gaming activities or are performed in a building housing such activities.

3. Empowerment zones (secs. 1393(a)(4) and 1391(g)(3)(E))

Empowerment zones generally provide tax incentives for businesses that locate within certain geographic areas designated by the Secretaries of the Departments of Housing and Urban Development (“HUD”) and Agriculture. The targeted areas are those that have a condition of pervasive poverty, high unemployment, and general economic distress, and that satisfy certain eligibility criteria, including specified poverty rates and geographic size limitations. Empowerment zone designations generally remain in effect through December 31, 2011.¹²⁴ The tax incentives include the empowerment zone employment credit, increased expensing under section 179, enterprise zone facility bonds, rollover of gain from the sale of empowerment zone assets, and an increased exclusion of gain from the sale or trade of qualified small business stock.

There have been three rounds of empowerment zone designations. The Omnibus Budget Reconciliation Act of 1993 authorized the designation of nine empowerment zones (“Round I empowerment zones”) and 95 enterprise communities to provide tax incentives for businesses to locate within targeted areas designated by the Secretaries of HUD and Agriculture.¹²⁵ The Taxpayer Relief Act of 1997 (“1997 Act”) authorized the designation of two additional Round I urban empowerment zones, and 20 additional empowerment zones (“Round II empowerment zones”). The Community Renewal Tax Relief Act of 2000 authorized a total of nine new empowerment zones (“Round III empowerment zones”). Indian reservations were not permitted to qualify for the Round I designations.¹²⁶ However, Indian reservations could be nominated for

¹²² Sec. 45A(c)(2) and (3). See IRS Form 8845, Indian Employment Credit (Rev. December 2011).

¹²³ Sec. 45A(c)(5).

¹²⁴ Sec. 1391(d).

¹²⁵ The empowerment zone and enterprise community rules are found in sections 1391-1397 of the Code.

¹²⁶ Sec. 1393(a)(4). The Omnibus Budget Reconciliation Act of 1993, which created empowerment zones, separately provided tax incentives for investment on Indian reservations. See sec. 168(j) (accelerated depreciation

Rounds II and III.¹²⁷ Part of Jackson County and all of Bennett and Shannon Counties in South Dakota comprise the Oglala Sioux Tribe Empowerment Zone.¹²⁸

4. Renewal communities (secs. 1400E(a)(1)(B)(ii), 1400E(a)(5) and 1400E(c)(2)(C)(ii))

The Community Renewal Tax Relief Act of 2000 authorized the designation of 40 “renewal communities” for which special tax incentives are available.¹²⁹ Indian reservations are eligible for designation as a renewal community.¹³⁰ The designation of an area as a renewal community terminated after December 31, 2009.¹³¹ While the majority of the tax incentives terminated after December 31, 2009, one tax incentive remains. The capital gain exclusion for renewal community assets is available for qualified capital gain attributable to periods on or before December 31, 2014.¹³²

Under section 1400F, gross income does not include any qualified capital gain from the sale or exchange of a qualified community asset held for more than five years.¹³³ For purposes of this provision, a qualified community asset means any qualified community stock, qualified community partnership interest, and any qualified community business property acquired after December 1, 2001 and before January 1, 2010.¹³⁴ Qualified capital gain means any gain recognized on the sale or exchange of a capital asset or property used in the trade or business (as defined in section 1231(b)).¹³⁵ Qualified capital gain shall not include any gain attributable to periods before January 1, 2002, or after December 31, 2014.¹³⁶

for property on Indian reservations) and sec. 45A (Indian employment credit), Pub. L. No. 103-66, sec. 13321 and sec. 13322, respectively.

¹²⁷ Secs. 1391(g)(3)(E) and 1391(h)(3).

¹²⁸ Internal Revenue Service, Publication 954, *Tax Incentives for Distressed Communities* (January 2004), p. 4.

¹²⁹ Community Renewal Tax Relief Act of 2000, Pub. L. No. 106-554 (December 21, 2000).

¹³⁰ An area can become a renewal community only after a process of nomination and designation as provided in the Code. Sec. 1400E. Certain differences exist with respect to the nomination and designation process and area requirements for Indian reservations. Secs. 1400E(a)(1), (5).

¹³¹ The designation would terminate earlier than December 31, 2009, if (1) an earlier termination date is so designated by the State or local government, or (2) the Secretary of HUD revokes the designation as of an earlier date.

¹³² Sec. 1400F(c)(2).

¹³³ Sec. 1400F(a).

¹³⁴ Sec. 1400F(b)(1).

¹³⁵ Sec. 1400F(c).

¹³⁶ Sec. 1400F(c)(2).

5. Credit for the production of Indian coal (sec. 45)

A credit is available for the production of Indian coal sold to an unrelated third party from a qualified facility for a seven-year period beginning January 1, 2006, and ending December 31, 2012. The amount of the credit for Indian coal is \$1.50 per ton for the first four years of the seven-year period and \$2.00 per ton for the last three years of the seven-year period (adjusted for inflation; \$2.267 per ton for coal sold in 2012).¹³⁷

A qualified Indian coal facility is a facility placed in service before January 1, 2009, that produces coal from reserves that on June 14, 2005, were owned by a Federally recognized Indian tribe or were held in trust by the United States for an Indian tribe or its members.

The credit is a component of the general business credit,¹³⁸ allowing excess credits to be carried back one year and forward up to 20 years. The credit cannot be used to reduce alternative minimum tax liability.

¹³⁷ 77 Fed. Reg. 21835, 21836 (April 11, 2012).

¹³⁸ Sec. 38(b)(8).

**E. Exclusion From Income and Employment Taxation of Income Derived
by Indians From Exercise of Fishing Rights (sec. 7873)**

Income derived from treaty recognized fishing rights-related activity by a member of an Indian tribe or a qualified Indian entity is excluded from income and employment taxes.¹³⁹

¹³⁹ Sec. 7873. This provision was enacted by the Technical and Miscellaneous Revenue Acts of 1988, Pub. L. No. 100-647, sec. 3041(a) (November 10, 1988).

**F. Exemption from Federal Unemployment Tax for Employment
by Indian Tribes (secs. 3306(c)(7), (u), and 3309(d))**

Under the Federal Unemployment Tax Act (“FUTA”), employers must pay a tax equal to six percent on total wages paid with respect to covered employment. Indian tribes, like State or local governments, may elect to pay FUTA taxes only when a former employee claims unemployment benefits. Only then does such electing employer have FUTA tax liability. Generally, the FUTA liability due equals the amount of such benefits claimed. Thus, for FUTA tax purposes, Indian tribes are treated the same as State and local governments. For purposes of the election, Indian tribe is defined as including any subdivision, subsidiary, or business enterprise wholly owned by the Indian tribe.¹⁴⁰ An Indian tribe may make a separate election for itself and each subdivision, subsidiary, and business enterprise wholly owned by the Indian tribe.¹⁴¹

¹⁴⁰ Sec. 3306(u).

¹⁴¹ This exemption was enacted by the Community Renewal Tax Relief Act of 2000, Pub. L. No. 106-554, sec. 166(a)(1)-(2) (December 21, 2000). This exemption does not apply when the Indian tribe is merely a “statutory employer”—that is, the entity having control of the payment of wages. *Blue Lake Rancheria v. United States*, 653 F.3d 1112 (9th Cir. 2011) (Court reversed and remanded District court and held that the common-law employer (wholly owned by the Indian tribe) was the employee leasing company as opposed to the client to whom the workers were leased, and thus, the employee leasing company was entitled to the exemption from employment taxes as an instrumentality of the Indian tribe).

G. Charitable Contribution Deduction for Certain Expenses in Support of Native Alaskan Subsistence Whaling (sec. 170(n))

In general, no charitable contribution deduction is allowed for a contribution of services. However, unreimbursed expenditures made incident to the rendition of services to an organization contributions to which are deductible may constitute a deductible contribution.¹⁴²

Effective for contributions made after December 31, 2004, a special rule permits a charitable deduction not exceeding \$10,000 per taxable year for certain expenses incurred in carrying out sanctioned whaling activities.¹⁴³ The deduction is available only to an individual who is recognized by the Alaska Eskimo Whaling Commission as a whaling captain charged with the responsibility of maintaining and carrying out sanctioned whaling activities. The deduction is available for reasonable and necessary expenses paid by the taxpayer during the taxable year for: (1) the acquisition and maintenance of whaling boats, weapons, and gear used in sanctioned whaling activities; (2) the supplying of food for the crew and other provisions for carrying out such activities; and (3) the storage and distribution of the catch from such activities.¹⁴⁴

For purposes of this special rule, the term “sanctioned whaling activities” means subsistence bowhead whale hunting activities conducted pursuant to the management plan of the Alaska Eskimo Whaling Commission.¹⁴⁵

¹⁴² Treas. Reg. sec. 1.170A-1(g).

¹⁴³ Sec. 170(n). This provision was enacted by the American Jobs Creation Act of 2004, Pub. L. No. 108-357, sec. 882(b) (October 22, 2004).

¹⁴⁴ Sec. 170(n)(2).

¹⁴⁵ Sec. 170(n)(3).

III. BACKGROUND STATISTICS ON NATIVE AMERICANS

A. Overview

Although Native Americans make up less than one percent of the U.S. population, they make up a much larger percentage of the population in States in the West, Southwest, Northern Plains and Alaska. Native Americans are unique as an ethnic group because they are eligible to live on reservations – tracts of lands set aside by the government for Native Americans to live and maintain their culture. Thirty percent of Native Americans live on reservations.¹⁴⁶

Native Americans¹⁴⁷ generally earn lower income and have higher unemployment rates than other households in the United States. The average unemployment rate among Native Americans was 17.9 percent in 2009.¹⁴⁸ Among those Native Americans living on Indian reservations,¹⁴⁹ the unemployment rate was 49 percent.¹⁵⁰ In 2010, the median income of Native American households was \$35,062; this number is 29 percent lower than the median income of the overall U.S. population, \$50,046.¹⁵¹

¹⁴⁶ Census Bureau (2012), *The American Indian and Alaska Native Populations by Selected Tribal Groupings: 2010*. Detailed Tables B02001 and B02010.

¹⁴⁷ In this section, the term “Native Americans” is used interchangeably with “Indians,” “American Indians,” and also “American Indians and Alaskan Natives.” For the purposes of this analysis, the term “Native Americans” refers to those who self-identify as “American Indian and Alaskan Native” in the census, and who do not identify as any other race.

¹⁴⁸ Joint Committee staff calculation based on Census Bureau, *2010 American Community Survey Data*, Table S2301.

¹⁴⁹ For purposes of this section, the term “Indian reservation” refers to tracts of land as described by the Census Bureau and the Department of Interior.

¹⁵⁰ Department of the Interior, Bureau of Indian Affairs, Office of Tribal Services (2005), *The American Indian Population and Labor Force Report: 2005*, p. 39.

¹⁵¹ Census Bureau, *2010 American Community Survey Data*, Table S1903.

B. Proportion of Native Americans in the U.S. Population

In 2010, American Indians and Alaskan Natives constituted 2.9 million people in the United States, less than one percent of the total population. However, another 2.3 million Americans affirm they are both Native American and another race, making a total of 5.2 million Americans (1.4 percent) who identify as all or part Native American.¹⁵² Excluding Pacific Islanders, Native Americans are the smallest minority group recorded by the U.S. Census.

Most Native Americans are affiliated with one or more specific Federally recognized Indian tribes; as of 2010, Navajo (286,627), Cherokee (284,229), and Sioux (112,102) are the most populous Indian tribes in the United States.¹⁵³ On the other end of the spectrum, there are also some very small Indian tribes with fewer than 100 members. Figure 1 aggregates all Indian tribes that make up less than four percent of the total Native American population into one large group, including all Alaskan Natives such as Eskimo, Aleut, and Inuit. Tribal affiliations are important because Federal and tribal benefits are often linked to formal tribal membership.¹⁵⁴

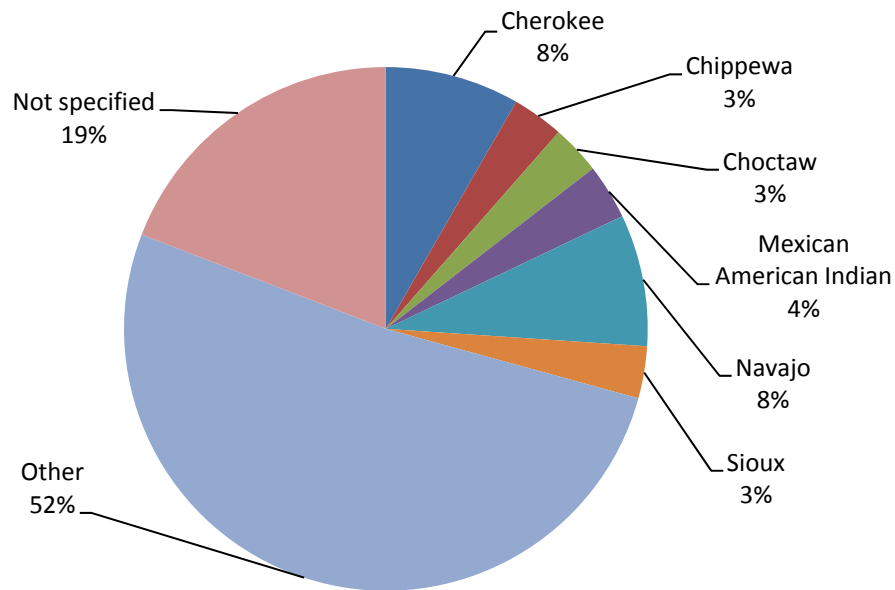
¹⁵² Census Bureau (January 2012), *The American Indian and Alaska Native Population: 2010*, p. 3.

¹⁵³ Census Bureau (January 2012), *The American Indian and Alaska Native Population: 2010*, p. 17.

¹⁵⁴ In spite of this link, 19.1 percent of Native Americans did not specify their Indian tribe in the 2010 Census.

Figure 1, below, displays the percentage of Native Americans by tribal affiliation. The Cherokee and Navajo are the two largest single Indian tribes, but the vast majority of Native Americans are in much smaller Indian tribes or are unaffiliated with any Indian tribe.

Figure 1.—Percentage Distribution by Tribal Affiliation in 2010



Source: Census Bureau, *American Indian and Alaska Native Populations by Selected Tribal Groupings: 2010*.

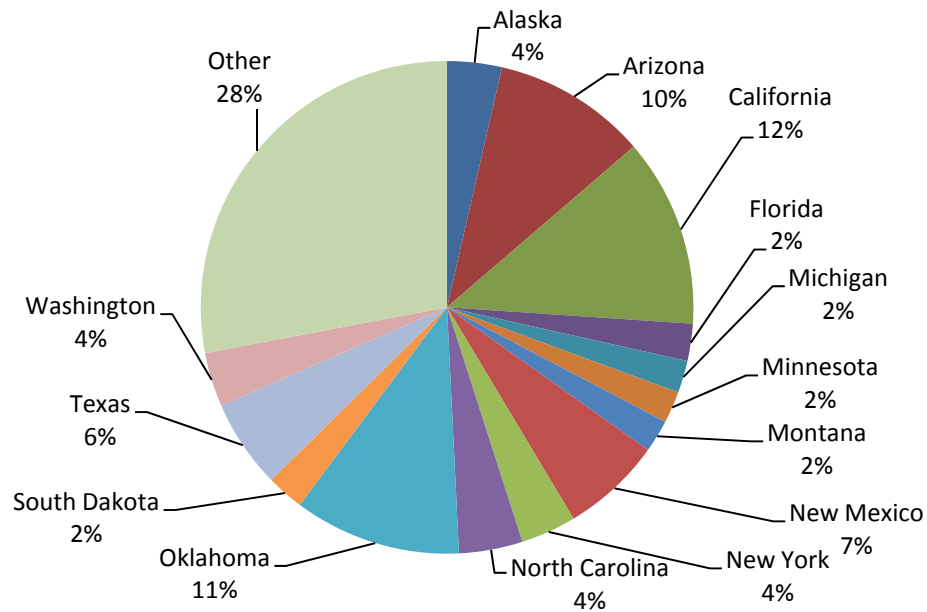
Note: The term “Mexican American Indian” indicates people of indigenous ancestry to Mexico, not regions in the United States.

C. Geographic Distribution of Native Americans in the United States

Figure 2 shows the State of residence of the total U.S. Native American population. Approximately 12 percent of all Native Americans live in California; however, Native Americans comprise less than one percent of the total State population. Only four percent of the country's Native Americans live in Alaska, but they comprise nearly 13 percent of the State's population.

Figure 2 also shows that approximately one-third of all Native Americans reside in three States: Arizona, California and Oklahoma. The Native American population is most concentrated in the West, Northern Plains, and Southwest, with more than five percent of the total American Indian population living in each of the following States: Arizona, California, New Mexico, Oklahoma, and Texas.

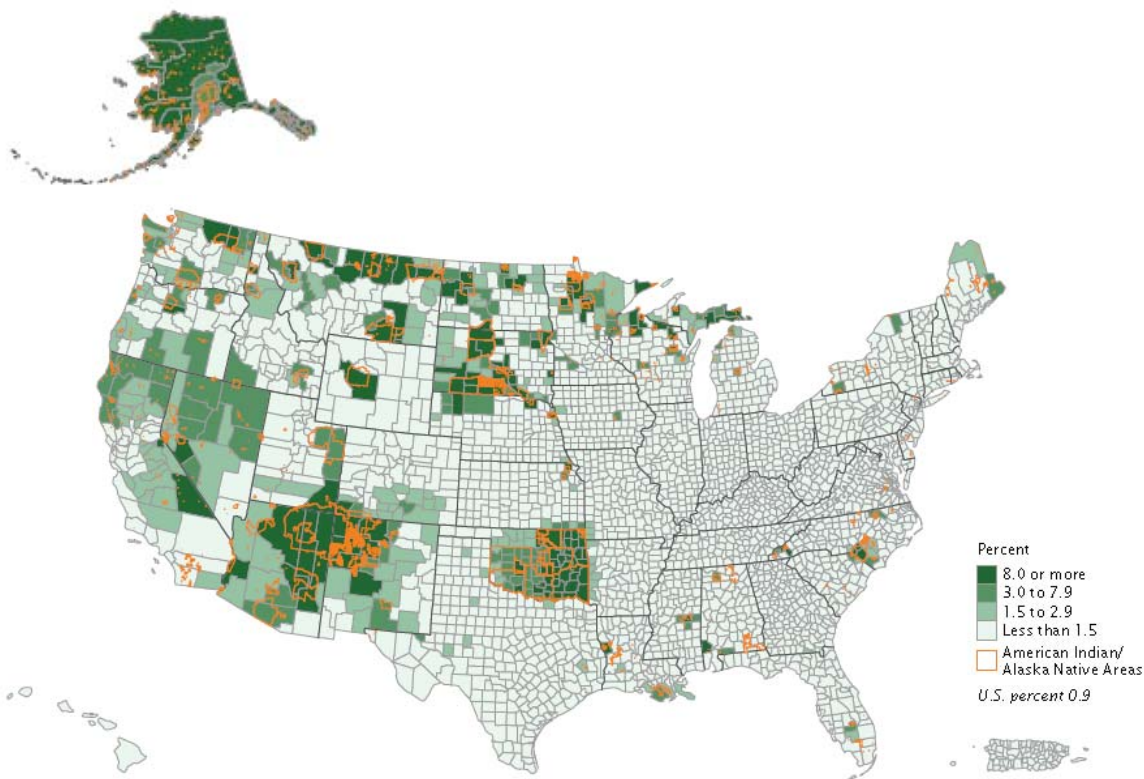
Figure 2.—Distribution of Native American and Alaskan Native Population by State of Residence in 2010



Source: Census Bureau, *American Indian and Alaska Native Populations for the United States, Regions, and States and for Puerto Rico: 2000 and 2010*.

Figure 3 shows the Native American population rate as a percentage of county population. This map further reinforces the fact that the Native American population is concentrated in the West, Northern Plains, Southwest, and Alaska.

Figure 3.—Native American Population as a Percentage of County Population in 2010



Source: Census Bureau, *2010 Census Redistricting Data (Public Law 94-171) Summary File*, Table P1.

Native Americans are the most rural of minority populations. While many other minority populations are heavily clustered in urban areas and States with high percentages of the populations located in urban areas, Native Americans mostly live in rural regions in the West, Northern Plains, Southwest, and Alaska. Approximately 30 percent of all Native Americans live on reservations.¹⁵⁵ The majority of Native Americans (70 percent) do not live on reservations. The proportion of Native Americans living on reservations varies greatly by state. In Oklahoma, nearly half of all Native Americans live on reservations, while in Arizona, fewer than three percent of all Native Americans live on reservations.¹⁵⁶

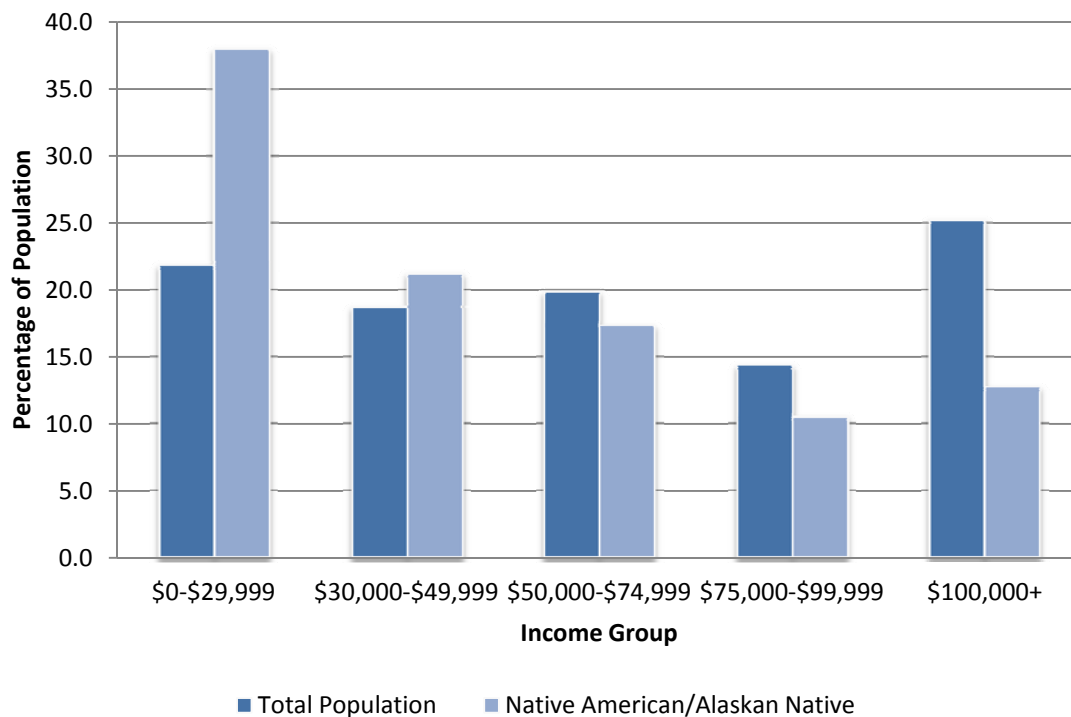
¹⁵⁵ Census Bureau, *2010 Census Redistricting Data (Public Law 94-171) Summary File*, Table P1.

¹⁵⁶ Census Bureau (2000), *Population Living on Selected Reservations and Trust Lands*, Table 38.

D. Economic Status of Native Americans

According to the census, the median income of a Native American household in 2010 was \$35,602, 22 percent lower than the median income in South Dakota (\$45,669) and 18 percent lower than the median income of Oklahoma (\$43,400),¹⁵⁷ two States with relatively high percentages of Native Americans. The median income for Native Americans is 29 percent lower than the median income for all U.S. households (\$50,046).¹⁵⁸ Figure 4, below, shows the income distribution of Native American households relative to the total population. The greatest differences in the income distribution are at the extremes. Native Americans are almost twice as likely as the rest of the population to earn under \$30,000 per year (38 percent versus 21.8 percent) and approximately half as likely (12.7 percent versus 25.2 percent) to earn more than \$100,000 per year.

Figure 4.—Income Distribution of Native Americans and Non Native Americans in 2009



Source: Joint Committee staff calculation based on the Census Bureau (2012), *Selected Characteristics of Racial Groups and Hispanic/Latino Population: 2010*, Table 36.

Note: “Total Population” refers to the total U.S. population, including American Indians and Alaskan Natives.

¹⁵⁷ Census Bureau, *2010 Annual Social and Economic Supplement to the American Community Survey*, Table H-8.

¹⁵⁸ All income amounts are expressed in 2010 dollars.

Much of the income differential may be driven by the extremely high rates of unemployment on reservations and among Native Americans in general. In 2005, 49 percent of those living on reservations and eligible to work were unemployed and 29 percent of this same population were employed but had annual earnings below the poverty line. Seventy-eight percent of Native Americans living on reservations were either unemployed, or employed with earnings that left them below the poverty line.

High unemployment, paired with low average income, yielded a 27-percent poverty rate in Native American populations in 2009 compared with a 14-percent poverty rate in the white population.¹⁵⁹ The differential is greater for children, with 31 percent of Native American children living in households in poverty, relative to 11 percent of children in impoverished households in the rest of the population. In the over-65 population, 20 percent of Native Americans are in poverty compared to only seven percent of the white, over-65 population in poverty.

Occupational choice among employed Native Americans is similar to that of the rest of the population as shown in Table 1, below. There are some differences, with relatively more Native Americans performing service jobs (24.6 percent versus 17.8 percent in the total population) and construction jobs (12.2 percent versus 8.7 percent), and fewer Native Americans in management and professional occupations (25.7 percent versus 35.7 percent).

Table 2.—Percent of Workers Older Than 16 Years Employed in Certain Occupations in 2009

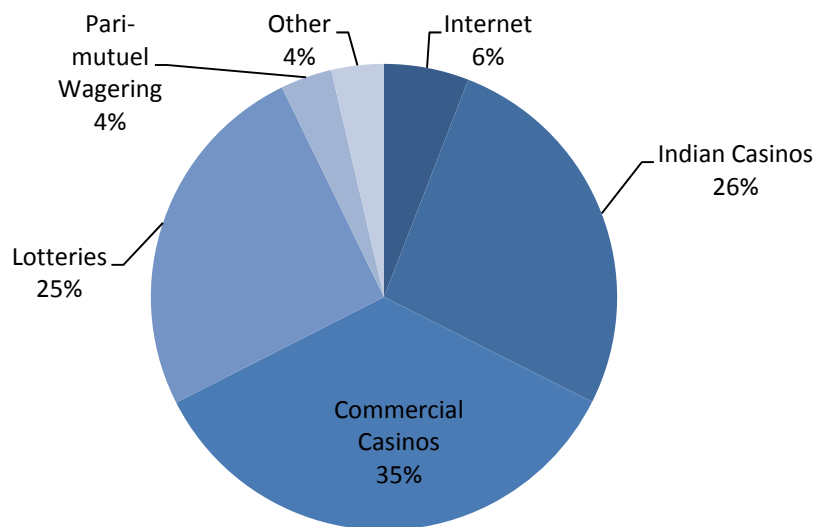
Occupation	Total Population	Native American/Alaskan Native
Management, professional and related occupations	35.7	25.7
Service occupations	17.8	24.6
Sales and office occupations	25.2	22.7
Farming, fishing, and forestry occupations	0.7	1.3
Construction, extraction, and maintenance occupations	8.7	12.2
Production, transportation, and material moving occupations	11.9	13.5

Source: Joint Committee staff calculation based on the Census Bureau (2012), *Selected Characteristics of Racial Groups and Hispanic/Latino Population: 2010*, Table 36.

¹⁵⁹ Census Bureau (2012), *Selected Characteristics of Racial Groups and Hispanic/Latino Population: 2010*, Table 36.

In 1987, the U.S. Supreme Court issued a decision barring the state of California from applying its regulatory statutes to gambling activities on Indian reservations. In 1988, Congress passed the Indian Gaming Regulatory Act (“IGRA”).¹⁶⁰ IGRA provides for the use of revenues from gambling to promote economic development and welfare of Indian tribes. Since 1988, casinos have become an important source of revenue for some Native American tribal governments. Figure 5 shows Indian casinos accounted for 26 percent of total revenue from gambling in 2007.

Figure 5.—U.S. Gambling Revenue in 2007



Source: Christianson Capital Advisors.

Note: “Other” includes: card rooms, legal bookmaking, charitable games.

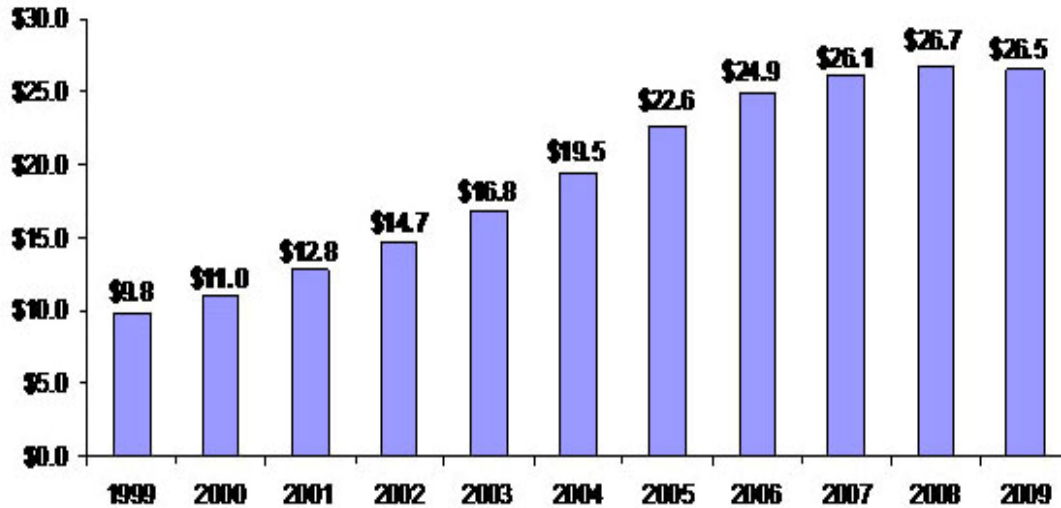
Pari-mutuel wagering includes horse racing, dog racing, and jai-alai.

In 2009, 233 individual Indian tribes engaged in gambling activities in 28 states, generating revenue totaling \$26.5 billion.¹⁶¹ Figure 6 shows a near-tripling of revenues from Indian gaming operations between 1999 and 2009.

¹⁶⁰ Pub. L. No. 100-497.

¹⁶¹ Press Release, National Indian Gaming Commission, “2009 Indian Gaming Revenues Remain Stable,” June 11, 2010, available at http://www.nigc.gov/Media/Press_Releases/2010_Press_Releases/PR-126_06-2010.aspx.

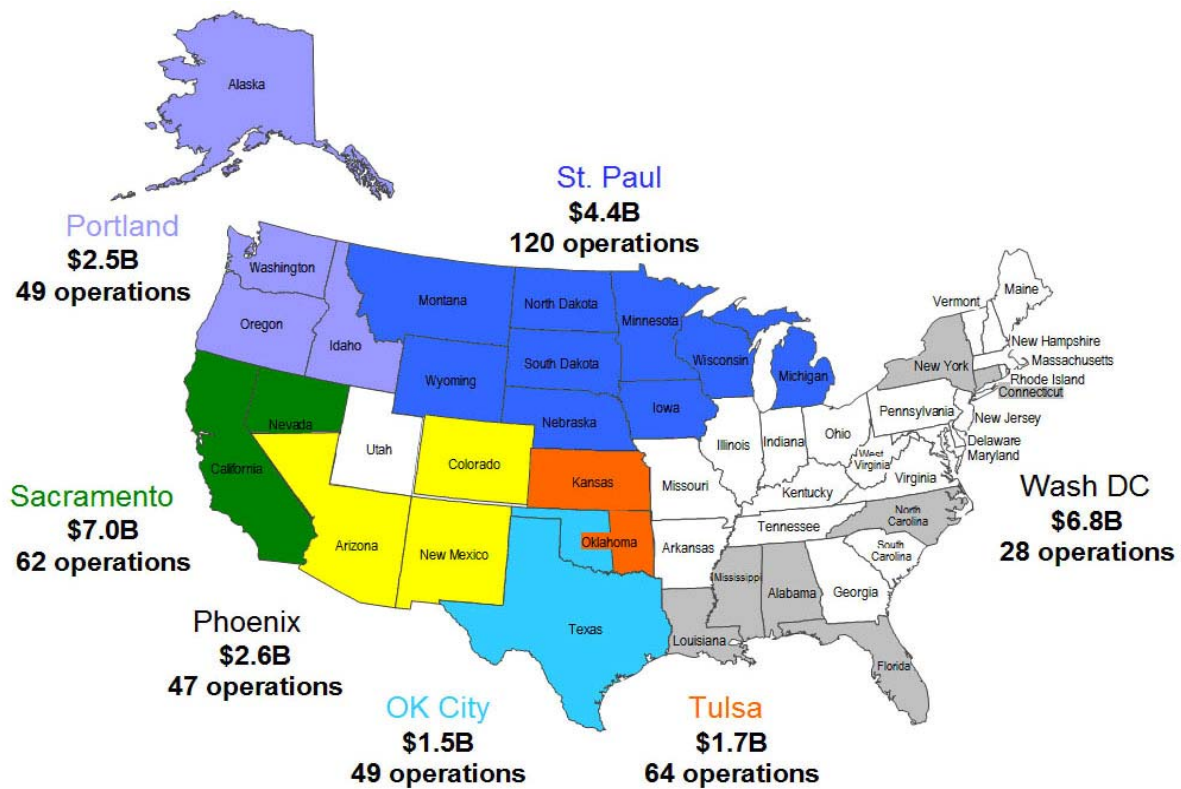
**Figure 6.—Total Revenues from Indian Gaming Operations
in the U.S., 1999-2009
(Billions of Dollars)**



Source: National Indian Gaming Commission.

Figure 7 shows the distribution of Indian gaming revenues across States in 2009 by reporting regions. The largest total revenues were generated in California and northern Nevada; and States in the Washington, D.C. reporting region.

**Figure 7.—Distribution of Revenues from Indian Gaming Operations Across Regions, 2009
(Billions of Dollars)**



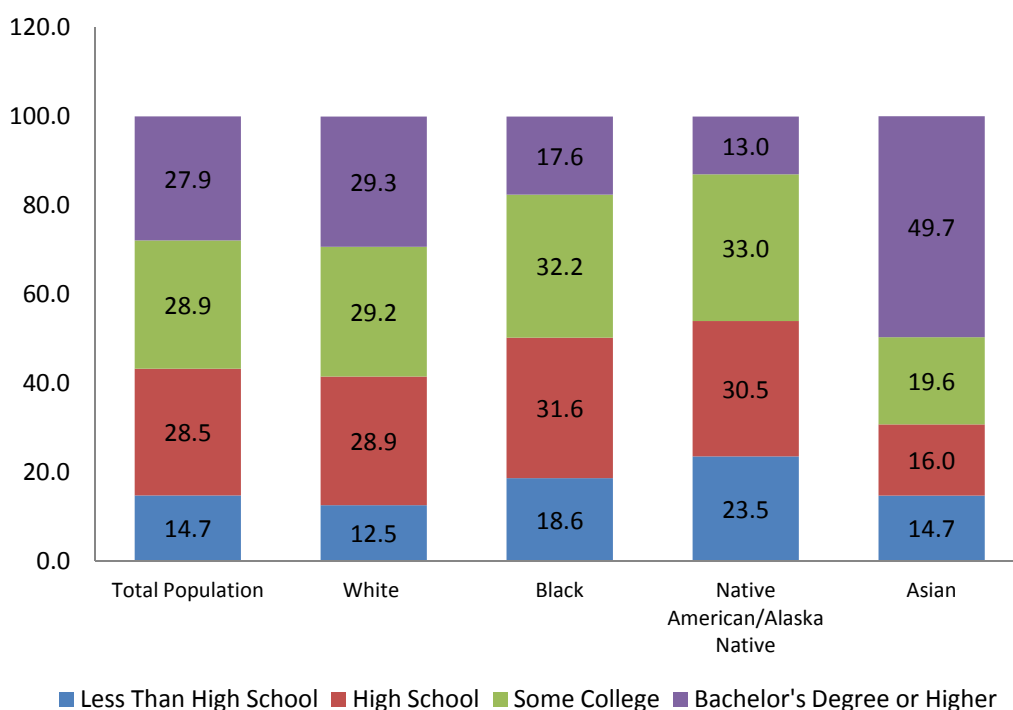
Source: National Indian Gaming Commission.

Note: In this figure, states are divided into seven reporting regions as shown. Gambling revenues are aggregated and reported across these regions.

E. Educational Attainment of Native Americans

Educational attainment is lower for Native Americans than it is for all other racial groups in the United States. In 2009, fewer than 15 percent of Native Americans received a bachelor's degree or higher, less than half the rate of the total population. In addition, in 2009, 23.5 percent of all Native Americans did not complete high school or high school equivalency compared to 14.7 percent of whites, 18.6 percent of blacks, and 14.7 percent of Asians.¹⁶² Figure 5 shows the breakdown of educational attainment by race in 2009. Native American educational attainment was lower than the educational attainment of blacks, whites, or Asians, with the lowest rates of post-high school education and the lowest rates of college graduation relative to these groups.

Figure 8.—Top Educational Achievement by Race in 2009



Source: Joint Committee staff calculation based on the Census Bureau (2012), *Selected Characteristics of Racial Groups and Hispanic/Latino Population: 2010*, Table 36.

¹⁶² Joint Committee staff calculation based on the Census Bureau (2012), *Selected Characteristics of Racial Groups and Hispanic/Latino Population: 2010*, Table 36.

F. Indian Health Service and Health Status of Native Americans

All people who can reasonably claim Native American heritage are entitled to care through the Indian Health Service (“IHS”). Generally, this is limited to Native Americans living on or near a reservation. However, IHS services are limited by budget constraints. Most recently, the average funding of an IHS site was found to be 40 percent less than an equivalent average health insurance plan.¹⁶³ Among all Native Americans, 35 percent are uninsured.¹⁶⁴ Fifty-five percent of Native Americans rely on the IHS’s 49 hospitals and 600 other health facilities for care.¹⁶⁵

Table 3.—Major Diseases with Significantly Greater Incidence in Native Americans Populations

Disease	Likelihood of Disease Relative to the Rest of the Population
Alcoholism	6.1
Tuberculosis	6.0
Diabetes	2.8
Unintentional Injuries	2.4
Homicide	1.9
Suicide	1.8
Cervical Cancer	1.4
Infant Mortality	1.2

Note: Data for American Indian and Alaska Natives 2004-2006 and U.S. All Races 2005.

Source: Department of Health and Human Services: Indian Health Service, *Fact Sheet, 2004-2006*.

The life expectancy of a Native American born today is 5.2 years less than the U.S. average life expectancy (72.6 years vs. 77.8 years, respectively).¹⁶⁶ Certain diseases have far greater prevalence in the Native American community than in the rest of the community. According to Table 3, alcoholism and tuberculosis are approximately six times more prevalent among Native Americans than the total U.S. population. Similarly, diabetes, unintentional injuries, homicide, suicide, cervical cancer, and infant mortality, are also more prevalent among Native Americans than in the total U.S. population.

¹⁶³ Department of Health and Human Services, Indian Health Service (January 2007), *Personal Health Services Funding Disparities*.

¹⁶⁴ The Kaiser Family Foundation (February 2004), *American Indians and Alaska Natives: Health Coverage and Access to Care*.

¹⁶⁵ Department of Health and Human Services, Indian Health Service (January 2006), *Facts on Indian Health Disparities*.

¹⁶⁶ Department of Health and Human Services, Indian Health Service (January 2007), *Fact Sheets*.