



# State Taxation of Tribal Businesses

By Tanya Gibbs and Jennifer Saeckl

Federally recognized tribes and, by extension, their wholly owned and operated arms and instrumentalities including their businesses, occupy unique status under taxation laws. Because federally recognized tribes are sovereign entities, they possess all the inherent rights of sovereign entities such as state governments, including the right not to be taxed. However, this right is not so straightforward, and taxation of tribal businesses may be affected by the type of tax, the level of government attempting to assert its taxation authority over a tribal business, and the corporate structure of the tribal business.

At the federal level, the Internal Revenue Service has concluded that federally recognized tribes are not subject to federal income taxation.<sup>1</sup> This exemption extends to and covers tribally owned businesses that are operated directly by the tribe as an arm of the tribe, regardless of whether the income is earned on or off tribal land.<sup>2</sup> However, unless they are specifically exempted from a federal taxation regime, tribes are generally treated as states for other federal taxation purposes.<sup>3</sup> Also, unless an exemption otherwise

exists, individual tribal members are still responsible for paying federal income taxes.<sup>4</sup>

The application of state law, however, is more muddled. While states may not assess taxes directly on tribes or tribal members for on-reservation activity,<sup>5</sup> the United States Supreme Court has upheld state taxation in instances when tribes or tribal businesses engage in certain off-reservation business or when tribal members earn income off the reservation.<sup>6</sup> However, the Supreme Court has also held that a state may not impose its taxes on a tribe or tribal business when the state tax is preempted by federal statute or when the tax infringes on a tribe's ability to "make [its] own laws and be ruled by them."<sup>7</sup>

In many cases, the taxability of a tribal business (or the strength of its arguments for or against taxability) can depend on the structure of the business. For example, an unincorporated division or arm of a tribal government that is integral to the tribal government's operation is generally not subject to federal taxation.<sup>8</sup> Similarly, tribal corporations chartered under federal law, such as those organized under Section 17 of the

Indian Reorganization Act, benefit from certainty of exemption from taxation under federal law.<sup>9</sup> However, a tribal corporation formed under state law is taxable under federal law even when it is wholly owned by the tribe.<sup>10</sup> The same may not be true for tribal limited liability companies formed under state law, assuming a tribe is the sole member. This is because the income or loss of the limited liability company “flows through” to its sole member—the tribe—which would be a tax-exempt entity.<sup>11</sup> Finally, while tribal businesses organized under tribal law can be firmly under the tribe’s sovereign control and therefore not subject to federal taxation, they lack the certainty of that status, which applies to, for example, Section 17 corporations.

In Michigan, many federally recognized tribes have entered into tribal-state tax agreements to clarify the boundaries of their taxation obligations to the state (and vice versa), create firm commitments in areas where taxation authority may be unclear, and uphold their government-to-government relationships with the state of Michigan.<sup>12</sup> When a tax agreement between the tribe and the state is unclear, federal caselaw regarding applicability of state taxation law should apply to determine if the state can exercise its taxation authority over the tribe.

## Business and corporate taxes

Tribal organizations conducting business on tribal lands are exempt from income taxation. However, if business is conducted off tribal lands, taxability depends on the business structure and the applicable tribal-state tax agreement.

## Sales and use taxes

Tribal businesses are generally exempt from sales tax within the area specified in the tribal-state tax agreement so long as a tax-exempt certificate is provided. Tribal businesses operating within the defined area per the tribal-state tax agreement still charge sales tax to their patrons (although there are certain exemptions related to fuel and tobacco for tribal members) and then split the sales tax between the tribe and the state of Michigan based on the terms of the agreement.

## Income taxes

Under the relevant state law, the Income Tax Act, revenue generated by a tribe or tribal business solely on tribal land is exempt from taxation. However, the Supreme Court has permitted states to tax income earned off reservation land, and Michigan imposes income tax on income earned by Indians off the reservation.<sup>13</sup> A tribe’s specific tax agreement may cover income tax and likely will assist with determinations of apportionment between on- and off-reservation income.

## AT A GLANCE

**Businesses that are owned by federally recognized tribes occupy a unique space in taxation schemes, particularly within state taxation schemes. This unique space is further complicated by differences in corporate structure, taxation schemes, and negotiated agreements between tribes and states. Tribes and tribal businesses must continue to negotiate on a government-to-government basis with the state to clarify the contours of state taxation while tribal economic development continues to diversify and expand.**

## Real property taxes

Land owned in trust by the United States for the benefit of a tribe may not be taxed by the state.<sup>14</sup> Thus, Michigan’s property tax statute, the General Property Tax Act, does not apply to trust real property.<sup>15</sup> Land owned in fee outside of the reservation or tribal lands may be subject to the General Property Tax Act or may be negotiated under a tax agreement.

## Personal property taxes

Taxation of personal property owned by tribes or tribal businesses has not been explicitly addressed. The General Property Tax Act provides an exemption from personal property taxes only when negotiated in a tax agreement and involving property used exclusively on tribal lands.<sup>16</sup> A tribe’s tribal-state tax agreement should determine personal property taxation.

However, if a tribe or tribal business’s off-reservation personal property does not meet the requirements for an exemption under the state law or is not discussed in its tribal-state tax agreement, basic Supreme Court principles should be applied to determine if the state may exercise its taxation authority. Courts will resolve the issue in favor of the tribe so as not to limit tribal sovereignty.<sup>17</sup> In applying that rationale to a tax agreement, silence regarding personal property taxation does not confer jurisdiction upon the state of Michigan to tax a tribe.

Moreover, the United States Supreme Court has held that state and local authorities may not impose taxes on personal property owned by tribes or tribal members.<sup>18</sup> Thus, personal property owned by tribes or tribal businesses may not be taxed under a state taxation regime.

## Taxation of tribes and tribal businesses is complicated by differences in corporate structure, taxation schemes, and the existence of tribal-state tax agreements.

### Conclusion

Taxation of tribes and tribal businesses is complicated by differences in corporate structure, taxation schemes, and the existence of tribal-state tax agreements. Tribes and their businesses should continue to monitor developments in federal law regarding taxation and work with the state to ensure their tribal-state tax agreement helps to clarify the application of state taxes. This is particularly true given the evolving landscape of tribal business ventures and the diversification of tribal economic development. ■



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### ENDNOTES

1. Rev Rul 67-284, 1967-2 C.B. 55; Rev Rul 81-295, 1981-2 C.B. 15; Rev Rul 94-16, 1994-1 C.B. 19.
2. Rev Rul 67-284, 1967-2 C.B. 55.

3. 26 USC 7871.
4. *Squire v Capoeman*, 351 US 1, 6; 75 S Ct 611; 100 L Ed 883 (1956) and *Choteau v Burnet*, 283 US 691; 51 S Ct 598; 75 L Ed 1353 (1931).
5. *McClanahan v Arizona State Tax Comm'n*, 411 US 164; 93 S Ct 1257; 36 L Ed 2d 129 (1973).
6. *Mescalero Apache Tribe v Jones*, 411 US 145, 149; 93 S Ct 1267; 36 L Ed 2d 114 (1973) and *Oklahoma Tax Comm'n v Chickasaw Nation*, 515 US 450, 465; 115 S Ct 2214; 132 L Ed 2d 400 (1995).
7. *Washington State Dep't of Licensing v Cougar Den*, 586 US \_\_\_\_; 139 S Ct 1000 (2019) (holding that the imposition of a Washington fuel importation tax was preempted by the Yakama Nation's treaty right to travel on public highways) and *Williams v Lee*, 358 US 217, 220; 79 S Ct 269; 3 L Ed 2d 251 (1959).
8. Rev Rul 94-16.
9. *Id.*
10. *Id.*
11. 25 CFR 301.7701-3(b)(1) and Rev Rul 2004-50, 2004-1 C.B. 977 (holding that "[a] federally recognized Indian tribal government is not an eligible S corporation shareholder for purposes of IRC § 1361.").
12. Mich Dep't of Treasury, *State/Tribal Tax Agreements and Amendments*, available at <[https://www.michigan.gov/taxes/0,4676,7-238-43513\\_43517--,00.html](https://www.michigan.gov/taxes/0,4676,7-238-43513_43517--,00.html)> [<https://perma.cc/4UKP-ELVQ>] and Executive Directive 2012-2 <[https://www.michigan.gov/documents/snyder/ExecutiveDirective2012-2\\_396160\\_7.pdf](https://www.michigan.gov/documents/snyder/ExecutiveDirective2012-2_396160_7.pdf)> [<https://perma.cc/H9Q3-RH9Y>]. All websites cited in this article were accessed June 13, 2019.
13. *Oklahoma Tax Comm'n v Chickasaw Nation*, 515 US 450, 465; 115 S Ct 2214; 132 L Ed 2d 400 (1995) and Mich Dep't of Treasury RAB 1988-47, available at <[https://www.michigan.gov/treasury/0,4679,7-121-44402\\_44415\\_44416-7363--,00.html](https://www.michigan.gov/treasury/0,4679,7-121-44402_44415_44416-7363--,00.html)> [<https://perma.cc/C5LS-NUBM>].
14. *McClanahan v Arizona State Tax Comm'n*, 411 US 164; 93 S Ct 1257; 36 L Ed 2d 129 (1973).
15. MCL 211.1 *et seq.*
16. MCL 205.30c(12)(d)(i).
17. *Merrion v Jicarilla Apache Tribe*, 455 US 130, 152; 102 S Ct 894; 71 L Ed 2d 21 (1982) ("[A]mbiguities in federal law have been construed generously in order to comport with the...traditional notions of sovereignty and with the federal policy of promoting tribal independence.") (citing *White Mountain Apache Tribe v Bracker*, 448 US 136, 143-144; 100 S Ct 2578; 65 L Ed 2d 665 (1980)).
18. See, e.g., *Moe v Salish & Kootenai Tribes*, 425 US 463, 480-481; 96 S Ct 1634; 48 L Ed 2d 96 (1976) (holding that a state could not levy personal property tax on motor vehicles owned by tribal members who lived on reservation); *Bryan v Itasca Cty*, 426 US 373, 377; 96 S Ct 2102; 48 L Ed 2d 710 (1976) (holding that Itasca County did not have authority to levy personal property tax on a tribal member's mobile home located on trust land); and *Washington v Confederated Tribes of Colville Indian Reservation*, 447 US 134, 163; 100 S Ct 2069; 65 L Ed 2d 10 (1980) (holding that the state may not "impose personal property taxes on property owned by...Indians.")