



California Indian Legal Services (CILS) Community Legal Education Self-Help Series

Bishop ♦ Escondido ♦ Eureka ♦ Sacramento

Native American Taxation Issues for California Taxpayers

► What's in this guide and how can it help me?

The focus of this packet is California state income tax issues raised when filing such individual returns with the Franchise Tax Board. Even among Native American taxpayers different rules may apply. The information contained in this packet, while specific to Native Americans, is general in scope and your particular tax situation may contain issues outside of this packet.

⇒ **Tip:** Taxpayers should feel free to take a copy of this packet with them when visiting their tax preparer and share the information if the taxpayer feels it may apply to their situation. Those taxpayers using online tax preparation services may also wish to have this packet with them at the time they are completing their online returns.

⇒ **Tip:** This guide also explains the meaning of some legal terms that appear in bold and are defined at the end in a section called "Some Helpful Terms" that starts on page [6](#).

1. As a Native American, do I need to pay individual income tax?

Yes. Native American must pay *federal* income tax to the IRS. There are no 'treaty' exemptions from federal income tax. Certain Native American trust assets and income from some class action lawsuit settlements are not taxable, however, these situations are uncommon. See the question covering per capita payments for further information. [Internal Revenue Bulletin: 2006-15, April 10, 2006, Rev. Rul. 2006-20](#). As to whether you also need to pay *state* income tax, see the next question.

2. I am Native American so when do I not need to pay state income taxes?

It depends. In some situations enrolled members of California federally recognized tribes do not need to pay state income taxes on income earned while living and working on their own tribe's reservation. If such taxes have been withheld by an employer the tribal member is entitled to receive that money back. If the taxpayer only lived on the reservation for part of the year then he or she would be exempt from state income taxes for that period, provided all the conditions listed above are met.

This state income tax exemption does not apply to Native Americans from tribes outside the state living in California, Native Americans who belong to California tribes but work off of their tribe's reservation, and Native Americans from non-federally recognized tribes. For those who are exempt from state income taxes, it does not matter if their income derives from wages or honorarium or per capita payments; all forms of income are exempt.

3. I live and work on my own reservation and my employer withheld state income taxes. What do I do to get this money back?

If you have not yet filed your income tax return, you will need to speak with your tax preparer about filing a California adjustment with your state return to reflect that you were not subject to state income tax. If you use an online tax preparation software, you will need a program that allows you to enter California adjustment. Typically tax preparers and programs use [FTB form 540 Schedule CA](#) (California adjustments form) to record the adjustment. This Schedule CA can be used when filing for the refund of the current tax season. If you were assessed state income tax for a prior tax year where you already filed a return, you will need to file an amended state return showing the adjustment.

4. In years past FTB stated that I had to show that my income came from a 'reservation source income' to get the exemption. Is this still correct?

No. In the past, the FTB maintained that a tribal member's income must come from a "reservation source" to be exempt from state income tax. The FTB's position however was inconsistent with the Supreme Court's decision on this issue in *McClanahan v. Arizona State Tax Commission*. Due in part to the efforts of Indian law practitioners the FTB decided that income earned on the reservation by tribal members living there was exempt from state income tax regardless of the source (e.g. tribal government, private employer, etc.).

For those who were assessed such taxes due to FTB's former interpretation, you can ask for a refund of state income tax withheld for the last four years by filing an amended return and printing RESERVATION SOURCE INCOME at the top of the return. For more details see the FTB's webpage:

https://www.ftb.ca.gov/individuals/Native_Americans/Reservation_Source_Income.shtml

5. I only lived and worked on my own reservation for part of the year. Am I entitled to a refund of all the state income taxes withheld on my W-2?

State income tax is not assessed for those months where the taxpayer/tribal member both lived and worked on his or her own reservation. State income tax is, however, assessed for the remainder of the year. You will need to calculate the number of months where you lived and worked on your own reservation/Indian country and only request a refund for state income tax withheld for that period only. Months where you did not both live and work on your own reservation/Indian country will be subject to state income taxation.

6. I receive different types of per capita payments from my tribe. Are they all taxable?

Many are taxable and a few are not. Gaming per capita payments, including Revenue Trust Fund Sharing payments, are always subject to federal income taxation. This is regardless of whether the tribe withholds taxes; if they do not withhold taxes, the taxpayer will still be liable for such taxes which may result in circumstances where the taxpayer owing both state and federal income tax.

In recent years the federal government has settled a number of federal court litigation cases - providing one-time cash settlements to hundreds of Native individuals. Many of these settlements are exempt from both federal and state taxation. [Indian Tribal Judgment Funds Use or Distribution Act, Pub. L. No. 93-134, 87 Stat 466, 25 U.S.C. §§ 1401-1408](#). Please note that only the settlement amounts are exempt. If, during the administration of the settlement payment, the money was provided from the federal government to the tribes and the tribes paid out the settlements to members *in excess of the settlement amount*, then that extra amount is considered as gross income but the amount of the settlement per cap it not. For a list of tribes who have entered into settlements and further discussion as to determining the non taxability from Indian settlements, see [Internal Revenue Bulletin 2013-3](#).

Also exempt from both federal and state income taxes is income derived by individual members of Indian tribes, or by a qualified Indian entity, from fishing rights-related activity. See Internal Revenue Code [§ 7873](#).

7. I receive payments from the federal government and/or my tribe from the use of my Indian trust land. Is that money taxable?

Income directly derived by an Indian allottee from restricted allotted land held in trust by the United States federal government is NOT subject to federal or state income taxes. Indian trust land is often leased for a variety of purposes. It is not uncommon for such land to be leased or mined as proceeds to be derived such as rentals (including crop rentals), royalties, proceeds from the sale of the natural resources of the land, income from the sale of crops grown upon the land and from the use of the land for grazing purposes, and income from the sale or exchange of cattle or other livestock raised on the land. Such income is generally exempt from taxation. See [Revenue Ruling 67-284](#). Also see, 25 U.S.C. § 117b(a) and 25 U.S.C. § 1407.

8. What is an informational return and when do I need to file one?

An informational return is a tax return that contains information required to be reported to federal and state tax authorities even though the taxpayer may not owe any taxes. A common example is a taxpayer filing a state income tax return in a situation where the taxpayer lived and worked on their own reservation/Indian country and was thus not subject to state income tax but files a state informational return to provide this information to the FTB. Filing an informational return in these instances can help the taxpayer avoid the situation where the FTB mistakenly assesses taxes and penalties because it has no contradicting information and believes that the taxpayer owed state income tax.

9. I received an honorarium or stipend from my tribe for work I did for the tribal council. Do I need to report this income?

A stipend received by a tribal council member for their work on the council is taxable (and reportable) as income. However, the stipend/honorarium is not considered wages; no employer had to withhold any taxes such as FICA, FUTA, SDI etc. This is in keeping with [Revenue Ruling 59-354](#). The ruling makes clear that "...amounts paid to members of Indian tribal councils for services performed by them as council members do not constitute 'wages'". However, payments are still considered part of the taxpayer's gross income and as the Revenue Ruling states, unless a specific federal tax statute or treaty or agreement with the Indian tribe concerned says otherwise, the income is taxable. It may be taxable as state income as well.

10. I've been hearing a lot about needing to show that I have health care coverage or I will be fined on my taxes. Where can I get more information about this?

The IRS has a short but informative booklet describing the changes and potential reporting requirements that you will need to know before you file your income tax returns. See IRS [Publication 5187](#), Health Care Law: What's New for Individuals & Families.

11. I am Native American and I've heard I can get an exemption from having to show that I have health care coverage. How does that work?

CILS has separate health care exemption materials including the exemption application form for those who need to receive an *exemption certificate number* before they file a federal income tax return. Those eligible for an ECN must show they are a member of a federally recognized tribe or eligible for Indian Health Services. They should also not be eligible under Medi-Cal or a qualified private or Marketplace insurance plan. For more information, ask CILS about this exemption or go to: <https://marketplace.cms.gov/applications-and-forms/tribal-exemption.pdf>

12. Last year I made below the required amount to have to file income tax returns. Do I still need to file a return to show proof of insurance?

Taxpayers whose gross income is below the minimum threshold for filing an income tax return are exempt from the shared responsibility provision and do not need to file an income tax return to show their insurance coverage or exemption. But if a taxpayer made below the minimum threshold and wants to receive a tax refund, they will be required to claim a coverage exemption on their income tax return paperwork. Such low-income taxpayers will need to file [Form 8965](#), part II.

13. Do I need to have an ECN before I file my income taxes?

No! In fact, you can claim the exemption on [Form 8965](#), part III. Members of federally-recognized Indian tribes, including an Alaska Native Claims Settlement Act (ANCSA) Corporation Shareholder (regional or village), or for those who were otherwise eligible for services through an Indian health care provider or the Indian Health Service can use Exemption Type E. If, however, the IRS flags your return for follow up, you may be asked to provide

evidence of Indian Health coverage and/or membership in your tribe. For instructions on filling out Form 8965 see the [instruction booklet](#).

14. I have my ECN and I am filing my own taxes. Where do I put my Native American exemption information?

You will need to report your ECN on [Form 8965](#), part I. For instructions on filing out Form 8965 see the [instruction booklet](#).

15. What documents do I need to have ready before I prepare my taxes or visit my tax preparer?

Ask your tax preparer or review the online tax software requirements prior to beginning your tax preparation but do not forget to have ready your ECN, if you have one. Also if you are visiting a tax preparer do not forget to describe the source of your tribal income and do not forget to bring this packet along and mention any issues that might pertain to your situation.

⇒ **TIP:** To locate a tax preparer in your area, visit the Voluntary Income Tax Assistance (VITA) program in your area: <http://irs.treasury.gov/freetaxprep/> or call 800-906-9887. Seniors may use the AARP Site Locator Tool: <http://www.aarp.org/applications/VMISLocator/searchTaxAideLocations.action> or call 888-227-7669.

Additional Reading:

[Per Capita Distributions of Funds Held in Trust by the Secretary of the Interior, IRS Notice 2014-17](#)

[January 2015 Edition of Indian Tribal Government News -scroll down to see article, "Reporting Tribal \(per capita\) distributions on your 2014 tax returns"](#)

⇒ **TIP:** For additional general resources on Native American taxation issues you may wish to consult our handout, State Taxation & Native Americans or visit the Internal Revenue Service (IRS) website: <http://www.irs.gov> and the FTB webpage on Income Taxation of Native Americans: https://www.ftb.ca.gov/individuals/Native_Americans/index.shtml

✧ Some Helpful Terms ✧

Bureau of Indian Affairs (“BIA”) – A federal agency within the Department of the Interior charged with managing Indian trust lands. In California the Pacific Regional Office is charged with all non education-related Bureau programs, functions and activities. The Regional office oversees four agency offices that provide services at the local level: Northern California, Central California, and Southern California, and Palm Springs. Information about the various California BIA agencies can be found at: <http://www.bia.gov/WhoWeAre/RegionalOffices/Pacific/index.htm>

Exemption Certificate Number (or ECN) – A number issued by the Marketplace which shows the taxpayer is exempt from having to demonstrate they have health coverage through the Marketplace.

Federally recognized tribe – A Tribe eligible for funding and services from the Bureau of Indian Affairs (BIA) in a government-to-government relationship with the United States. The [Federal Register](#) lists all the federally recognized tribes in the country on an annual basis.

Indian Country – Refers to any of the following: all lands within an Indian reservation or Rancheria; Indian allotments, the Indian titles to which have not been extinguished; and dependent Indian communities within the US under the jurisdiction of the federal government.

Indian Health Services - The Indian Health Service (IHS), an agency within the Department of Health and Human Services, provides federal health services to American Indians and Alaska Natives. In California the IHS tribal health programs operate clinics throughout the state but rely on private and public hospitals to meet inpatient hospital and emergency needs.

Per Capita Payments – Distributions of money made to members of federally recognized tribes. Such payments can come from the use of the individual Indian's trust asset, such as payment for leasing of their trust land or harvesting of timber. It can also derive from gaming and other tribal enterprises where the profits are shared by a tribe among their tribal members.

Tribal Affiliation – Refers to the tribe(s) or tribal group(s) that a person is associated with but not necessary a member of. An individual who is not yet a Navajo tribal member but who has information that leads them to believe they have Navajo ancestry may be said to affiliate themselves with Navajo, for example, but necessarily an official member of the Tribe.

Jan 2015

CILS Community Legal Education Self-Help Series

The Community Legal Education Self-Help Series is a project of CILS. The Series' mission is to expand access to legal resources that increase Indian self-sufficiency. This guide is part of our Community Legal Education Self-Help Series, providing Indians and Indian tribes with user-friendly information and self-help assistance pertaining to their legal status and rights. Community Legal Education Self-Help guides, and more information about CILS and California Indian issues, are available on our website at www.calindian.org.

California Indian Legal Services

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Do you have a legal problem? For assistance, contact your local CILS office:

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Escondido: (760) 746-8941, or toll-free at (800) 743-8941

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Sacramento: (916) 978-0960, or toll-free at (800) 829-0284

