

## TREASURY'S COMMENT PROJECT ON THE GENERAL WELFARE DOCTRINE OF TAX EXEMPTION

### *I. Introduction*

IRS audits and administration of the federal tax laws in Indian Country is always fraught with controversy. There is one particular internal revenue law that is the subject of most audits – the “general welfare doctrine” (GWD) or “general welfare exclusion” (GWE) from taxation. The GWE audit involves the IRS review of tribal government distributions to members for purposes of ascertaining the tribe’s compliance with Form 1099 information reporting, or withholding requirements. This has proved to be a costly and inefficient means for tribes (and the IRS) to determine whether tribal general welfare program benefits will subject members to taxation.

A general statement of the law does not provide much guidance. Internal Revenue Code (I.R.C.) Section 61 provides that, except as otherwise provided by law, gross income means all income from whatever source derived. Tribal income not otherwise exempt is includable in the gross income of the Indian tribal member when distributed or constructively received by them. Rev. Rul. 67-284. An administrative exception to the general rule of broad includibility of income has developed through IRS rulings and determinations, called the “general welfare doctrine” (GWD) or “general welfare exclusion” (GWE).

Under the general welfare doctrine, payments made by federal, state, local and Indian tribal governments under a legislatively provided social benefit program for promotion of the general welfare are excludable from gross income. The rule is stated as follows:

When a governmental unit makes payments to or for the benefit of an individual or family, in the absence of a disaster, governmental payments made without regard to financial status, health, educational background, or employment status do not qualify under the general welfare exclusion because they are not based on “need.”

Rev. Rul. 76-131 and Rev. Rul. 85-39.

Because the GWE is an administrative exemption that has evolved largely from rulings related to benefits provided by state and local governments, tribal governments have not been given sufficient notice of Treasury’s position on the taxability of *tribal* programs specifically. There is a paucity of rulings specific to tribes. And, IRS rulings in the form of Private Letter Rulings or Technical Advice Memoranda are non-precedential and technically cannot be relied upon by any other taxpayer or tribe. Further, the IRS position on GWE is inconsistent. For instance, some auditors have required a showing of individual financial need to support a GWE, but published rulings on state/local

government programs do not require such showing. See, e.g., Rev. Rul. 57-102; TAM 200035007. There is simply insufficient IRS guidance upon which tribes can rely to formulate their general welfare programs and policies.

## *II. Tribal Comments to Treasury*

In response to many inquiries from Indian tribal governments on this issue and in order to provide clarity and certainty to Indian tribal governments and consistency in applying the exclusion, the Service and the Treasury Department (pursuant to E.O. 13175) issued Notice 2011-94 on November 15, 2011 to invite comments describing actual or proposed Indian tribal government programs that provide benefits to members and the application of the exclusion to these programs and benefits. Although the comment period officially ended March 15, 2012, input from tribal governments continues to be considered, as of this date.

Numerous tribes and tribal associations have provided comments to Treasury. The overarching themes which emerge from the comments, are as follows:

1. IRS/Treasury should be held accountable to Executive Order 13175 which provides direction to Federal agencies on agency rulemaking:
  - Tribes request respect for Indian self-government and sovereignty and, where possible, defer to Indian tribes to establish standards to preserve the prerogatives and authority of Indian tribes as directed by the President;
  - Tribes request IRS/Treasury work with Indian tribes on a government-to-government basis and recognize the federal government's unique obligation to tribes – greater training of IRS employees on tribal governments is also requested.
2. The U.S. is a party to the United Nations Declaration on the Rights of Indigenous Peoples which recognizes that indigenous peoples have important collective human rights which necessitate special measures by the government to protect and preserve those rights:
  - Federal policies should, thus, encourage the preservation of tribal culture in accordance with the UNDRIP, not tax and punish tribal members actively participating in the preservation of their traditions and practices.
3. Acknowledge that IGRA mandates the provision of tribal programs and services as an aspect of self-government prior to taxable per capita payment to individual tribal members:
  - Also that federally approved revenue allocation plans (RAP) in accordance with IGRA should be respected – per capita reclassification by IRS violates IGRA RAP designations;

- Payments or services under a bona fide social benefit program are not per capita payments even if the benefits are provided on a community-wide or tribal-wide basis
4. Audits of Indian tribes are discriminatory on the basis that the same audits are not being conducted on state and local governments or foreign nations:
    - IRS agents should not substitute personal judgment for decisions that are made pursuant to a political process and form of government recognized by treaties, Congressional acts and Presidential Executive Orders spanning more than a century of tribal-federal relations;
    - While General Welfare Exclusion guidance is being developed, interim relief from the inconsistent application of the exclusion to Indian tribes under audit or subject to other enforcement actions should be provided.
  5. Tribal self-government traditionally includes housing assistance, education, child and elder care, and cultural preservation.
  6. The federal government should foster, not punish or interfere with, the provision of programs that address the unmet unique treaty and legal obligations.
  7. Tribal education services should never be subject to taxation by the United States because of the historical solemn promises made and unfulfilled and because tribal education policies always equate to general welfare.
  8. Individual means testing violates tribal culture and tradition and lack of means testing should not disqualify a tribal program from the exclusion when other eligibility criteria are present:
    - “Need” is not just financial and includes matters of health, educational background, employment status and others;
    - “Need” can be community based, such as high unemployment rates, lack of access to capital or disproportionate poverty levels;
    - “Need” can be cultural, such as programs that restore, protect, promote and extend tribal cultural heritage;
    - “Need” can be justified by programs that supplement or supplant federal funding or work towards the same goals of federal policy (even in the absence of federal funding);
    - “Social benefit” rather than “individual need” should be the primary focus, with deference to each tribal government in setting social goals and establishing programs to achieve them. Social benefit must encompass self determination and be construed broadly to reflect unique cultural and traditional-based programs and economic development.
    - Too much focus has been placed on individual means testing, and too little on the overall social benefit a program seeks to achieve.
    - Guidance must be broad and give substantial deference to the discretion of tribal governments and their legislative policy making process:
    - Each tribe has its own checks and balances in place for the approval of programs and those processes should be given deference;

- Tribal governments contain appropriate accountability mechanisms that are based on tribal community values, reciprocal responsibilities and programmatic objectives;
  - Tribes can identify shortcomings or abuse with an immediacy that federal agents will never attain;
  - Tribal governments should be acknowledged as partners in the tax compliance process and not as adversaries.
9. Benefits received pursuant to cultural programs should not constitute compensation for services when governmental assistance is tied to community service or job training programs.

### *III. Next Steps*

It is expected that government to government consultation on this issue will continue for some time. Although the official comment period is expired, I encourage tribes to continue to submit comments. In addition, in June 2012, the ACT (Federal Advisory Committee on Tax for Indian Tribal Government) will be making its recommendations on improvements to the administration of GWE in Indian Country.

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