

BEFORE THE STATE TAX APPEAL BOARD
OF THE STATE OF MONTANA

FLAT CENTER FARMS, INC.,)	
)	DOCKET NO: CT-1998-3
Appellant,)	
)	
-vs-)	
)	FINDINGS OF FACT,
THE DEPARTMENT OF REVENUE)	CONCLUSIONS OF LAW,
OF THE STATE OF MONTANA,)	ORDER AND OPPORTUNITY
)	<u>FOR JUDICIAL REVIEW</u>
Respondent.)	

The above-entitled appeal was set for hearing on May 5, 1999 in Glasgow, Montana. At the request of counsel for both parties, a telephonic pre-hearing conference was held on April 29, 1999. Both parties agreed that no substantive issues of fact remained in this case and that the matter could be submitted on briefs detailing the legal arguments. Accordingly, the May 5 hearing was vacated and a briefing schedule was developed. Final briefs were due on July 15. Having received briefs in a timely fashion from both parties, and having reviewed the briefs, the taxpayer's initial complaint, the Department of Revenue's answer to the complaint, and the Final Agency Order of the Department of Revenue, and being well and fully informed in the premises, the Board finds and concludes as follows:

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STATEMENT OF THE ISSUE

Flat Center Farms, Inc. (Flat Center) is a Montana corporation incorporated under the laws of Montana and doing business within Montana. The corporation is wholly owned by enrolled Indian persons. The taxpayer contends that, because the shareholders of the corporation are individually exempt from Montana corporate license tax due to their status as enrolled members of an Indian tribe, the corporation should also be afforded this exemption.

FINDINGS OF FACT

The parties stipulated and agreed upon the following facts:

1. Flat Center Farms, Inc. is a corporation incorporated under the laws of the State of Montana, incorporated on December 3, 1993. Flat Center Farms, Inc. is a "C" corporation.

2. Flat Center Farms, Inc. is also a tribally chartered corporation which was chartered by the Fort Peck Tribes as a Tribal Corporation on October 7, 1996.

3. Kim Murray is an enrolled member of the Fort Peck Tribes, enrollment number U07523. His wife, Denise Murray, is an enrolled member of the Turtle Mountain Chippewa, which is also served by the Fort Peck Reservation. Denise Murray's enrollment

number is 70-0175.

4. Kim Murray owns 200 shares of Flat Center Farms, Inc. and his wife, Denise Murray, owns 200 shares.

5. Flat Center Farm's sole business activity is farming.

6. Flat Center Farm's farming operation is located wholly within the exterior boundaries of the Fort Peck Reservation.

7. Flat Center Farm, Inc. rents real estate upon which it operates its farming operation. The land is owned as follows:

898.4 acres trust land, held in Trust for individual Indians or the Fort Peck Tribes;

419.5 acres deeded land, owned by various Indian persons, all of said lands being Located on the Fort Peck Indian Reservation;

481 acres owned by the United States Government in trust for Kim Murray.

8. These very same lands were previously farmed by Kim Murray individually. When farmed by Kim Murray individually, rather than through his Indian owned corporation, the income from said land was tax exempt.

TAXPAYER'S CONTENTIONS

Flat Center contends that since 1) the corporation is tribally chartered, 2) the corporate activity occurs solely on the Fort Peck Indian Reservation, 3) the sole owner is a tribal member, and 4) the sole beneficiaries of the income are Indian

persons, the income should remain exempt from state income tax.

In its opening brief, Flat Center cites the authority for state income tax exemption of individual income earned by an Indian person derived solely from reservation sources as McClanahan v. State Tax Commission of Arizona, 411 U.S. 164 (1973). This holding was adopted as the law of the state of Montana in 1978 by the Montana Supreme Court in LaRoque v. State of Montana, 315, 583 P.2d 1059 (1978). LaRoque also gave tax exempt status to non-enrolled Indian persons whose income was earned solely from on-reservation activity.

Flat Center emphasized that, in LaRoque, the Montana Supreme Court found that the "primary factor in limiting state jurisdiction is whether the activity occurred in 'areas set aside by treaty for the exclusive use and control of Indians'", Id. at 603. Thus, the LaRoque finding was that the physical site of the income-producing activity is the primary factor in determining exempt status.

Flat Center argued that the present case is analogous in that the status of the taxpayer, a corporation, is secondary to the fact that the income-producing activity took place wholly within the boundaries of an Indian reservation. As Indians earning income on the reservation, that income must be exempt from state taxation.

Further support for this conclusion was held in State

of Montana v. Bird, 252 Mont. 438, 829 P.2d 941 (1992) in which the Montana Supreme Court held that even the income of an Indian residing on the reservation, but earned while working on non-Indian land off the reservation is exempt when the income is derived from tribally owned minerals under the land. Flat Center argued that this opinion also found the situs of the activity to be the primary factor in determining tax exemption.

In Fatt v. Utah State Tax Commission, 884 P.2d 123 (1994), the Utah Supreme Court held that an Indian serviceman's Navy pay was exempt from state income tax when his domicile remained his reservation home even though he was actually living elsewhere while he served in the military. Flat Center argued that, if another court extends the exemption to income earned off reservation and to work obviously not related to on-reservation work, income earned from on-reservation work by a solely Indian owned and tribally chartered corporation should be exempt. The fact that the vast majority of the lands farmed by Flat Center are trust lands held by the United States government for Indian owners or the Fort Peck tribes lends further support for exemption, according to the taxpayer.

In summary, the taxpayer urged this Board to conclude that the income in dispute, which was exempt when Mr. Murray's farming operation was not incorporated, should remain exempt since the corporation was tribally chartered and solely owned by

Indian persons. This income was earned entirely within the exterior boundaries of the Fort Peck Indian Reservation and the sole benefactors of the corporation are the Indian shareholders, Kim and Denise Murray. The situs of the activity and the Indian status of the entity have coalesced and therefore the income is exempt.

DEPARTMENT OF REVENUE'S CONTENTIONS:

The Department of Revenue (DOR) contended that the major flaw in the taxpayer's argument in favor of exemption is its failure to recognize the difference between individual income and corporate income. The DOR argues that, because corporations are separate entities, with an identity separate from its creators, they are taxed under a different statutory scheme than individuals.

Montana's corporation license tax or fee is paid "for the privilege of carrying on business in this state," and applies to all corporations subject to taxation (Section 15-31-101 (3), MCA). The corporation license tax is based upon a percentage of a corporation's total net income for the preceding taxable year.

Section 15-31-101 (2), MCA, defines the terms "engaged in business" and "doing business" as both meaning "actively engaging in any transaction for the purpose of financial or pecuniary gain or profit."

The DOR concludes that Flat Center is subject to the

corporation license tax pursuant to Title 15, chapter 31 of the Montana Code Annotated because it is organized as a Montana corporation for the purpose of financial or pecuniary gain; because its transactions all occur within Montana; and because Flat Center is not an individual.

In response to Flat Center's argument that, because it is owned solely by Indians who are enrolled members of a federally recognized tribe, the income is exempt from taxation by the state, the DOR contends that a corporation "is a legal fiction that has a life of its own, separate and distinct from its creator or creators and its shareholders", citing Dartmouth College v. Woodward, 17 U.S. (4 Wheat) 518, 636, 657, 4 L.Ed. 629) in Black's Law Dictionary 180 (5th ed. 1983) which defines a corporation as:

[A]n artificial person or legal entity created by or under the authority of the laws of a state or nation . . . ordinarily consisting of an association of numerous individuals. Such entity . . . is regarded in law as having a personality and existence distinct from that of its several members . . .

The DOR cited case law (Moline Properties v. Commissioner of Internal Revenue, 319 U.S. 436 (1943)) to support the argument that a corporation is separate and distinct from its creator, shareholders and directors. In Moline, the United States Supreme Court held that a corporation was a separate

entity from its sole shareholder and must be taxed accordingly, stating a corporation "fills a useful purpose in business life . . . [and] so long as that purpose is the equivalent of business activity or is followed by the carrying on of business by the corporation, the corporation remains a separate taxable entity."

The DOR further argues that Indian status cannot be obtained simply because the shareholders and incorporator are Indian; rather, that status is obtained by an individual as an enrolled member of a federally recognized tribe or by being a member of an Indian community wherein the individual is recognized as an Indian.

Flat Center also makes the erroneous argument that, because it is recognized by tribal charter, it should be exempt from taxation by the state. The DOR counters this argument by pointing out that the tribe does not own Flat Center and that Flat Center was not incorporated under Section 17 of the Indian Reorganization Act. Tribal charter has no effect; it is merely a recognition that the corporation exists. The tribal charter was enacted after the incorporation under state law took place and the tribal resolution is clear that the action was taken to avoid Montana tax, rather than to effect a tribal self-governance program. The tribal charter was not done in place of the Montana incorporation, thereby replacing a state corporation with a tribally-chartered corporation.

Corporate organization under the Indian Reorganization Act (IRA) makes the corporation an extension of the tribe and, thus, not taxable by the state. IRA provisions allow a tribe to form a corporation to promote economic self-sufficiency or to provide financial support for social programs. The DOR asserts that Flat Center was formed for financial or pecuniary gain and not to promote tribal interests, thereby precluding the requisite connection to tribal interests to sustain exemption from state taxation.

The DOR included a copy of the Federal Internal Revenue Service Revenue Ruling 94-16 with its response brief. According to the DOR, this ruling that indicates Indian corporations organized under state law, as was Flat Center, are subject to federal taxation. Ms. Cross Guns writes: "The rationale supporting this ruling is that an organization created by state law is fundamentally different from one created under federal law, such as the IRA. 25 U.S.C. Section 477 (1993). According to the ruling, an Indian tribe maintains tax exempt status, and a tribal corporation formed under the IRA is also exempt. However, where a corporation is formed under state law, that organization, regardless of the Indian status of any of its members, is subject to federal taxation."

While Revenue Ruling 94-16 does not indicate whether a state may also tax a corporation which is comprised of Indian

members and was formed under state law, the DOR argues that case law supports a state's authority to apply a nondiscriminatory tax to an Indian-owned corporation formed under state law. ". . . a State can impose a nondiscriminatory tax on private parties with whom the United States or an Indian tribe does business . . ."

Cotton Petroleum Corp v. New Mexico, 490 U.S. 175 (1989). The DOR also cites Burnet v. Coronado Oil & Gas Co. 285 U.S. 393 (1932), Oklahoma Tax Commission v. Texas Co., 336 U.S. 342 (1949.) which served to establish and strengthen the Court's position that a state can impose a nondiscriminatory tax on private parties with whom the United States or an Indian tribe does business.

The DOR also argues that the fact that Montana corporate income tax is tied to federal corporate income tax (Section 15-31-113, MCA), is further supportive of its claim that Indian-owned corporations formed under state law are subject to state corporation tax in light of Revenue Ruling 94-16 discussed above.

The DOR also discusses the fact that Flat Center leases or rents all of the land it uses to farm. Ms. Cross Guns writes, "The owners of the land, whether it is held in trust or as fee land, are compensated for Flat Center's use of the land. One of those owners is Kim Murray. Mr. Murray incorporated Flat Center Farms. The corporation pays Mr. Murray, by way of the

federal government, for the corporation's use of that land. The lease money paid for use of the land, in fact, is income derived from the land. By leasing the land for its own uses, the corporation has created another legal fiction that acts as distance for the question of situs."

In summary, Ms. Cross Guns argues that Flat Center Farm's corporate income is subject to state taxation because ". . . a corporation is a legal fiction that creates an entity separate from its members, thus rendering the corporation incapable of obtaining Indian status. Without status as an individual Indian, the corporation's income is not exempt from taxation by the state. Furthermore, the issues of situs is rendered moot for two reasons: situs is only important where income is generated by an individual Indian, and situs is defeated where the landowner has contracted with a non-Indian entity for the use of that land."

DISCUSSION

The parties to this dispute appear to differ upon the importance of situs versus corporate status in the determination as to whether or not the assessment of Montana Corporation License Tax and interest for tax year ending October 31, 1994 was correct.

Flat Center argues that the situs (Indian trust land farmed by Kim Murray, shareholder in the corporation) is

governing in the determination of exemption from Montana corporate license tax. Flat Center contends that this income was earned entirely within the exterior boundaries of the Fort Peck Indian Reservation and the sole benefactors of the corporation are the Indian shareholders, Kim and Denise Murray. The situs of the activity and the Indian status of the entity have coalesced and therefore the income is exempt.

The DOR argues that the corporate status of Flat Center renders it subject to the state corporate license tax due to its contention that a corporation is legally recognized as an entity which is separate and distinct from its creator, shareholders and directors. Further, the DOR contends that Indian status cannot be obtained simply because the shareholders and incorporator are Indian; rather, that status is obtained by an individual as an enrolled member of a federally recognized tribe or by being a member of an Indian community wherein the individual is recognized as an Indian.

Upon review of the relevant case law, statutory law and arguments presented by both parties to the appeal, the Board finds merit in the arguments of the DOR. A significant amount of case law was presented in support of the argument that a corporation is a separate legal entity from its creators, owners or shareholders. Incorporation is a business decision which carries with it certain benefits to the incorporator, including

some degree of protection from legal action against its shareholders, directors, etc., and some tax and financial advantages. Flat Center's argument in favor of tax exemption for the corporation because the individual, Kim Murray, received exemption due to his status as an enrolled Indian fails.

Further, it has not been demonstrated that Flat Center Farms, Inc. was created to promote tribal interests. The record indicates that the purpose of Flat Center is for profit or financial gain through farming income. Business entities conducting nontribal business are not exempt from state taxation and is subject to Montana Corporation License Tax under Section 15-31-101, Montana Code Annotated.

Flat Center's argument that it should be exempt from state taxation because it is recognized by a tribal charter fails. The record does not indicate that any of the tribes served by the Fort Peck Indian Reservation own Flat Center. Further, it appears that the tribal charter is simply a recognition that Flat Center exists.

Flat Center argued for exemption due to the fact that the majority of the lands it farms are within the exterior boundaries of the Fort Peck Indian Reservation. This land is also held in trust by the federal government for Indian owners of the Fort Peck tribes (situs argument). The Board finds that the argument in favor of exemption due to situs fails because

Flat Center does not have status as an **individual** Indian and, thus, its income is not exempt from taxation by the state. Further, the record indicates that Flat Center has contracted with a non-Indian entity, via trust and deeded land, for the use of the land it uses to farm.

CONCLUSIONS OF LAW

1. The subject income is subject to Montana Corporation License Tax under Section 15-31-101, MCA.

2. Flat Center Farms, Inc., a corporation, does not have status as an individual Indian, by virtue of its status as a separate legal entity, and its income is not exempt from taxation by the state.

3. The appeal of the taxpayer is hereby denied and the decision of the Montana Department of Revenue is hereby affirmed.

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ORDER

IT IS THEREFORE ORDERED by the State Tax Appeal Board of the State of Montana that the taxes and interest assessed are properly due and owing.

DATED this ____ day of July, 1999.

BY ORDER OF THE
STATE TAX APPEAL BOARD

GREGORY A. THORNQUIST, Chairman

(S E A L)

JAN BROWN, Member

JEREANN NELSON, Member

NOTICE: You are entitled to judicial review of this Order in accordance with Section 15-2-303(2), MCA. Judicial review may be obtained by filing a petition in district court within 60 days following the service of this Order.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this ____ day of July, 1999, the foregoing Order of the Board was served on the parties hereto by depositing a copy thereof in the U.S. Mails, postage prepaid, addressed to the parties as follows:

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