United States Department of the Interior

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Memorandum

To: Field Solicitor, Twin Cities

From: Ann M. Spencer, Attorney-Adviser

Subject: Research Memo on Taxability of Reservation Lands Held by Indians in Fee

I. Introduction

An unresolved question of great importance is whether the states can tax land within reservation boundaries owned by Indians in fee. Recent cases have sharply limited the states' power to tax Indian property or activities on reservations. Legal principles supporting tax-exempt status for Indian fee land on the reservation have already been established. This memorandum is an attempt to synthesize those principles into a coherent argument for tax-exemption of such lands.

Before analyzing the legal principles, it is useful to remember the federal policies behind tax exemption for Indian lands. A comprehensive law review article on the subject has identified two such policies: encouraging self-sufficiency of individual Indians and maximizing the value of Indian lands. Comment, Indian Taxation: Underlying Policies and Present Problems, 59 Cal. L. Rev. 1261, 1270 (1971) (hereinafter Indian Taxation). I would add a third policy: strengthening tribal self-government. Tax immunities provide tribal governments with enhanced opportunity for economic development by increasing the value of tribal land. If the land is exempt from state taxes, the tribal government also has wider latitude to apply its own tax structure. In this way, the tribe obtains revenue for tribal purposes and gains experience in the management of resources. These policies have as much relevance to lands held in fee as they do to trust lands. Even with regard to encouraging individual Indians' self-sufficiency, tax-exemption of fee lands furthers the policy. It may help overcome the less-productive nature of much Indian land, which is often many miles from industrialized areas and of poor quality, and enable the Indian owner to realize maximum income from it.

Fee lands within the reservation are of two types: first, those lands which were never in trust status and passed to the present Indian owners through inheritance or purchase, and second, those lands which were originally allotted and for which U.S. fee patents were issued. The state tax exemption, as this

memorandum will show, should apply to both categories. However, 25 U.S.C.A. § 349 (West) must be considered in any discussion of lands which were once allotted and are now covered by fee patents. This memorandum will first discuss those principles applicable to both types of fee land, and then discuss the effect of 25 U.S.C.A. § 349 (West) on fee patented lands.

At various times, courts have based state tax exemption for Indian lands on three legal theories: tribal sovereignty, the federal instrumentality doctrine, and federal pre-emption. These theories, and their applicability to taxation of fee lands within the reservation, will be discussed in turn.

II. Tribal Sovereignty

Although less frequently cited than it once was as a rubric for evaluating the permissible extent of state power over Indians, the tribal sovereignty doctrine retains considerable vitality and usefulness. The leading tribal sovereignty case is Williams v. Lee, 358 U.S. 217 (1959). There, a non-Indian who owned a store on the Navajo reservation sued tribal members in state court for sums which he claimed they owed him. The defendants challenged the state court's jurisdiction over the action. The United States Supreme Court said that whether the state had jurisdiction depended on the effect of such jurisdiction on the tribe's ability to govern itself.

> Essentially, absent governing Acts of Congress, the question has always been whether the state action infringed on the right of reservation Indians to make their own laws and be ruled by them. 358 U.S. at 220. (emphasis added.)

After studying the pertinent treaties and the Navajo court system, the Court determined that the state did not have jurisdiction over the dispute. Noting that the states have no power over reservation affairs absent Congressional authorization, the Court said that ". . . to allow the exercise of state jurisdiction here would undermine the authority of the tribal courts over Reservation affairs and hence would infringe on the right of the Indians to govern themselves." 358 U.S. at 255. The Williams v. Lee test comes into play only if Congress has not spoken about the applicability of a specific state law. When Congress has authorized or prohibited a particular exercise of state power on the reservation, the Congressional decision controls.

Without Congressional authorization, state taxation of Indian fee lands on the reservation, like the state court jurisdiction considered in Williams v. Lee, supra, interferes in an unacceptable way with the tribe's self-government. The ability to tax is an attribute of sovereignty that Indian tribes possess, at least if their Constitutions give them taxing power. In Barta v. Oglala Sioux Tribe, 259 F.2d 553 (8th Cir. 1958), cert. denied, 358 U.S. 932 (1959), the Court upheld the right of the tribe to levy a tax on non-member lessees of trust land. The tribe's Constitution contained a grant of taxing power. The Court said, quoting Iron Crow v. Oglala Sioux Tribe of Pine Ridge Res., 231 F.2d 89, 99 (8th Cir. 1956):

> Inasmuch as it has never been taken from it, the defendant Oglala Sioux Tribe possesses the power of taxation which is an inherent incident of its sovereignty. 256 F.2d at 556.

Cf. Arizona ex rel. Merrill v. Turtle, 413 F.2d 683 (9th Cir. 1969) (extradition ordinance was within sovereign powers of tribe).

State taxation of reservation fee lands impedes tribal government in several ways. First, it limits the tribe's freedom to formulate its own tax system. While a tribe empowered to tax by its Constitution could technically impose its own tax in addition to state taxes, this might so burden the land that the owners would leave the reservation. Further loss of reservation residents is undesirable from the tribe's point of view, so the tribe might decline to tax fee lands rather than encourage exodus from the reservation. Second, and in part a facet of the first point, state taxation reduces the revenue which the tribe can obtain from reservation land. This, in turn, lessens the total tribal revenue available for economic development, education, and other tribal programs, and impairs the effectiveness of tribal government.

The availability of all reservation land as a source of tax revenue is particularly important in light of the unique value of land to Indian people. Not only does land have great cultural significance for Indians, but it is often the major, and sometimes the only, income-producing asset which the tribe owns. Inability to tax fee lands, whether actual or in practical effect, can result in great diminution of tax revenues for tribes with tax systems. The Flathead Reservation in Montana, for example, is split about half and half between trust and fee lands. See, Moe v. Confederated Salish and Kootenai Tribes of the Flathead Reservation, 425 U.S. 463 (1976). If the tribal government chose to adopt a taxing system, it could double its revenues if it taxed fee lands as well as trust lands.

In one of the recent leading cases on Indian tax immunities, McClanahan v. Arizona Tax Commission, 411 U.S. 164 (1973), the United States Supreme Court hinted that it might find taxes on individual Indians, presumably including property taxes, violative of tribal sovereignty under Williams v. Lee, supra. McClanahan, which will be discussed at greater length infra, challenged the state taxability of Indian income earned entirely on the reservation. Arizona claimed, inter alia, that the tax was consistent with the tribal sovereignty principle of Williams v. Lee, supra, because the tax was on individual Indians, not on the tribe. Although deciding that the income was immune from state taxation on other grounds, the Court said, "[i]n fact, we are far from convinced that when a state imposes taxes upon reservation members without their consent, its actions can be reconciled with tribal self-determination," 411 U.S. at 179. This statement indicates the Court's openness to a well-reasoned argument on tribal sovereignty grounds against state taxation of reservation fee lands, at least without the consent of Congress or the tribe itself. Furthermore, the McClanahan court also said that the Williams v. Lee test was intended to apply to situations involving non-Indians. This suggests that state taxation of Indians might not be permitted by the Court, even if no interference with tribal sovereignty were shown.

Tribal sovereignty, although not the touchstone for analyzing state power over reservations that it once was, is still useful in formulating an argument against state taxation of Indian fee lands. This theory is worth pursuing, particularly since the Supreme Court has indicated that it might be receptive to such an argument.

III. The Federal Instrumentality Doctrine

In the past, courts relied extensively on the so-called federal instrumentality doctrine to support exemption of Indians from state taxes. The theory is that state taxation of Indians is an impermissible burden on the realization of federal policies. The federal policies thought to be inhibited by state taxation are the maximization of the value of Indian land and, more generally, the economic development of Indian tribes, see Indian Taxation at 1276. The doctrine has seldom been used in recent Indian tax immunity cases, and will be discussed only briefly.

In many of the cases which invoked the federal instrumentality doctrine, the issue was tax immunity for non-Indian lessees of Indian lands. Probably because the courts felt that private, non-Indian corporations were benefiting from the doctrine, they began to uphold non-discriminatory state taxes on lessees of Indian lands.

One of the leading cases limiting the federal instrumentality doctrine is Oklahoma Tax Commission v. Texas Co., 336 U.S. 342 (1949). There, the Supreme Court sustained the application of Oklahoma's gross production and excise taxes to lessees of mineral rights on Indian lands. The Court relied on the principle set out in Helvering v. Mountain Producers Corp., 303 U.S. 376 (1938). That case held that the doctrine was not violated by a non-discriminatory tax where the burden on a government instrumentality was not direct and the impact on a government function was remote. The Court emphasized that the case did not affect the tax immunity of Indian lands themselves.

The federal instrumentality doctrine is of limited usefulness in an argument for tax exemption of Indian fee lands. Not only is it not in favor with modern courts, but it seems more relevant to taxation of the tribe, which may be thought of as a government instrumentality, than to taxation of individual Indians.

The doctrine has, however, been used occasionally to support tax exemption of individual Indians. In Pourier v. Board of County Commissioners of Shannon Co., 83 S.D. 235, 157 N.W.2d 532 (S.D. 1968), Indians had used the proceeds of their trust property and tribal loans to purchase cattle. The county attempted to levy a personal property tax on the offspring of the cattle. The court held that the tax was impermissible on the ground that it was inconsistent with the federal instrumentality doctrine. The court reasoned that, since the federal government had given the Indians the original property to promote the federal policy of economic self-sufficiency, a state tax would interfere with the realization of that policy.

The decline of the federal instrumentality doctrine in Indian tax cases was deplored in Indian Taxation. The doctrine had been eroded because courts perceived the impact of non-discriminatory taxes on a federal function as "remote." According to the comment-writer, however, this reasoning is not persuasive where Indian lands are involved. This is because the federal goal is economic development of Indian reservations. Therefore any state tax on business operating on Indian property interferes with the goal by decreasing the attractiveness of Indian reservations as business locations. The comment-writer would extend tax immunity to any business operating on the reservation. A fortiori, the federal instrumentality doctrine would invalidate a direct tax on Indian-owned fee land, since the value of the land would be thereby diminished and the owner's progress toward economic self-sufficiency slowed.

In spite of attempts to revive it, the federal instrumentality doctrine is not likely to be resurrected in Indian tax cases. Recently, the Supreme Court, in Mescalero Apache Tribe v. Jones, 411 U.S. 145, 151 (1973), stated that even tribal enterprises are not automatically instrumentalities of the government for tax immunity purposes. The Court, noting that federal instrumentality analysis is out of vogue in Indian tax cases, said that tax immunity is now considered to be a legislative question. The next section of this memorandum will discuss the relevance of Congressional action to tax immunity of Indian fee lands.

IV. Federal Pre-emption

In the most recent line of cases, the crucial question in analyzing Indian tax immunity is whether Congress has authorized state taxation. If, after a search of the applicable treaties and statutes the court finds no authority for state taxation then the state may not tax. Federal authority, absent Congressional consent, is exclusive. Only Congress or the tribe itself may tax the property or activity in question. This principle, as stated in the cases, applies to fee lands as well as trust lands and supports a state tax exemption for both.

Two companion cases, McClanahan v. Arizona Tax Commission, 411 U.S. 164 (1973) and Mescalero Apache Tribe v. Jones, 411 U.S. 145 (1973), explore taxation of Indian property on the reservation in depth. In McClanahan, supra, Arizona tried to impose an income tax on a reservation resident whose entire income was earned on the reservation. The Court, noting that Indians are generally free of state control unless Congress provides otherwise, looked at the relevant treaties and statutes and found that Arizona had no taxing jurisdiction:

> . . . by imposing the tax in question on this appellant, the state has interfered with matters which the relevant treaty and statutes leave to the exclusive province of the Federal Government and the Indians themselves. 411 U.S. at 165.

The Court carefully limited its holding to Indian income earned on the reservation.

Mescalero, supra, was a step toward clarifying the scope of Indian tax immunity. There, the Mescalero Apache Tribe operated a ski resort on land leased from the Forest Service outside reservation boundaries. The state attempted to tax the business's gross receipts and business-related personalty. The Supreme Court rejected the claim that the Federal Government has exclusive jurisdiction over

all Indian affairs, whether on or off the reservation. Since the business was off-reservation and the New Mexico enabling act permitted state taxation of Indians outside reservation boundaries unless otherwise forbidden by Congress, the Court held that the tribe had to pay the gross receipts tax.

As to the tax on personalty, however, the Court held it invalid. The Court based its reasoning on 25 U.S.C.A. § 465 (West), which provides that land acquired by the Secretary of the Interior for Indians is to be exempt from state and local taxation. The Court found that leasing the land with funds provided by the Federal Government brought it within the scope of § 465 tax immunity. Because the personalty was affixed to the realty, it was also immune from state taxes. The Court in Mescalero stated the basic principle underlying tax immunity of Indian income or property:

> . . . in the special area of state taxation, absent cession of jurisdiction or other federal statutes permitting it, there has been no satisfactory authority for taxing Indian reservation lands or Indian income from activities carried on within the boundaries of the reservation, and McClanahan v. Arizona State Tax Comm'n, supra, lays to rest any doubt in this respect by holding that such taxation is not permissible absent congressional consent. 411 U.S. at 148 (emphasis added)

See also Pourier v. Board of County Commissioners of Shannon Co., 83 S.D. 235, 157 N.W.2d 532, 534 (S.D. 1968) ("Taxation or exemption of Indians by either the Federal Government or by the state is a matter for Congressional resolution.")

Thus three determinative factors emerge from the cases. First, is the property or income which the state wants to tax owned by or earned by an Indian? Second, is the property located, or was the income earned, on the reservation? If the answer to both questions is yes, the property may not be taxed by the state unless a third question, whether Congress has authorized state taxation, can also be answered in the affirmative.

These factors also determine taxability of Indian property in states where Public Law 280, 28 U.S.C.A. § 1360 (West) applies. Public Law 280 gives certain states criminal, and to some extent, civil jurisdiction on Indian reservations. In Bryan v. Itasca County, 426 U.S. 373 (1976), the issue was whether Public Law 280 grants taxing jurisdiction to the states where it applies. Itasca County, Minnesota levied a personal property tax on a mobile home owned by an Indian living on the Leech Lake Reservation. Citing McClanahan and Moe, both supra, the Court framed the issue in terms of Congressional consent:

> Thus McClanahan and Moe preclude any authority in respondent county to levy a personal property tax upon petitioner's mobile home in the absence of congressional consent. Our task therefore is to determine whether [Public Law 280] constitutes such consent. 426 U.S. at 377.

The Court held that Congress did not intend Public Law 280 to be a grant to the states of taxing jurisdiction over reservation Indians.

None of the above cases limit their holdings to trust property. All speak of Indian property on Indian reservations without distinguishing between trust property and fee property. The conclusion is inescapable that, absent Congressional consent, lands owned by Indians in fee are exempt from state property taxes if they are located on the reservation.

Any other result would not make sense. Indian tax exemptions are based on the relationship between the Federal Government and reservation Indians, not on the character of the property. If the trust nature of the property were determinative then it would be difficult to see the rationale for McClanahan, supra, which exempted Indian income earned entirely on the reservation from state income taxes. McClanahan is devoid of any indication that the income was derived from trust property. It is inconceivable that any court would, in light of McClanahan, hold fee lands within the reservation taxable. Such a holding would mean that an Indian who ran an on-reservation business on fee land would not have to pay state income taxes on business proceeds but would have to pay real estate taxes on the land itself. That result is patently absurd.

It is clear that Indian fee lands are tax-exempt if Congress has not granted taxing jurisdiction to the states. Where land was once allotted and then fee patented by the Federal Government, we must consider whether 25 U.S.C.A. § 349 (West) constitutes congressional consent to state taxation. Analysis based on recent cases shows that it does not.

Title 25 U.S.C.A. § 349 (West) provides that, after the expiration of the trust periods and issuance of fee patents to the allottees, ". . . each and every allottee shall have the benefit of and be subject to the laws, both civil and criminal, of the State or Territory in which they may reside . . ." At any time before the expiration of the trust period, the Secretary of the Interior may, if he determines the allottee to be competent to manage his affairs, issue a fee simple patent " . . . and thereafter all restrictions as to sale, incumbrance, or taxation of said land shall be removed . . ." We must now consider whether this statute constitutes Congressional consent to state taxation of Indian-owned reservation lands for which U.S. fee patents have been issued.

Section 349 should not be interpreted as a grant of state power to tax individual parcels of fee-patented land. That interpretation would create "checkerboard" jurisdiction within each reservation, whereby state power to tax would vary with the ownership and origin of title of each parcel. "Checkerboard" jurisdiction is not only unwieldy, but is not in harmony with present federal policy toward Indians or with recent cases.

The United States Supreme Court rejected the concept of "checkerboard" jurisdiction in the criminal law context in Seymour v. Superintendent, 368 U.S. 351 (1962). In that case, an Indian resident of the Colville Reservation in Washington had committed burglary on land which, while within the reservation,

was owned in fee by a non-Indian. The state of Washington claimed that its courts had jurisdiction to try the defendant because the crime was not committed on Indian land. The Court pointed to the definition of "Indian Country" in 18 U.S.C. § 1151, which gives the federal courts exclusive jurisdiction over certain crimes on Indian reservations, and concluded that the definition included the land where the defendant committed the crime. The Court went on to say:

> . . . where the existence or nonexistence of an Indian reservation, and therefore the existence or nonexistence of federal jurisdiction, depends upon the ownership of particular parcels of land, law enforcement officers operating in the area will find it necessary to search tract books in order to determine whether criminal jurisdiction over each particular offense, even though committed within the reservation, is in the State or Federal Government. 368 U.S. at 358

The Court disapproved this unworkable "checkerboard" approach.

More recently, the Supreme Court addressed the "checkerboard" jurisdiction issue in a taxation case. In Moe v. Confederated Salish and Kootenai Tribes of the Flathead Reservation, 425 U.S. 463 (1976), the Court considered the applicability of state cigarette sales taxes, vendor license taxes, and motor vehicle taxes to Indian residents of the Flathead Reservation in Montana.

The Court found that the state did not have jurisdiction to impose these taxes on Indian reservation residents, citing Mescalero Apache Tribe v. Jones, supra, and McClanahan v. Arizona State Tax Comm'n, supra.

Montana contended, among other things, that § 6 of the General Allotment Act, 24 Stat. 388 (1887), the predecessor of 25 U.S.C.A. § 349 (West), constituted Congressional consent to Montana's taxation of fee patented Indian lands. The Court said:

> If the General Allotment Act itself establishes Montana's jurisdiction as to those Indians living on 'fee patented' lands, then for all jurisdictional purposes--civil and criminal--the Flathead Reservation has been substantially diminished in size. 425 U.S. at 478 (emphasis in original).

The Court refused to accept this proposition and, citing Seymour v. Superintendent, supra, rejected "checkerboard" jurisdiction in the tax context as it had in the criminal law context.

> Congress by its more modern legislation has evinced a clear intent to eschew any such 'checkerboard' approach within an existing Indian reservation, and our cases have in turn followed Congress' lead in this area. 425 U.S. at 479.