

PART I

Section 1361. – Small Business Corporation

26 CFR: 1.1361(b): Small business corporation defined.
(Also: §§ 401, 501, 1362, 7701, 7871, 305.7871-1.)

Rev. Rul. 2004-50

ISSUE

Is a federally recognized Indian tribal government, as described in § 7701(a)(40)(A) of the Internal Revenue Code, an eligible S corporation shareholder under § 1361?

FACTS

X is a federally recognized Indian tribal government (Indian tribal government) and a shareholder in Corporation, a domestic entity, formed in accordance with the laws of State. Corporation wants to make an election to be an S corporation.

LAW AND ANALYSIS

Section 1361(a) provides that for purposes of this title, the term “S corporation” means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for the year.

Section 1361(b)(1) provides that for purposes of this subchapter, the term “small business corporation” means a domestic corporation which is not an ineligible corporation and which does not (A) have more than 75 shareholders, (B) have as a shareholder a person (other than an estate, a trust described in subsection (c)(2), or an organization described in subsection (c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than one class of stock.

Section 1361(c)(6) provides that for purposes of subsection (b)(1)(B), an organization which is (A) described in §§ 401(a) or 501(c)(3), and (B) exempt from taxation under § 501(a), may be a shareholder in an S corporation.

Section 401(a) provides the definition of a qualified pension, profit-sharing, and stock bonus plans that qualifies under § 1361(b) as an eligible S corporation shareholder.

Section 501(a) provides that an organization described in subsection (c) or (d) or § 401(a) shall be exempt from taxation under this subtitle unless that exemption is denied under § 502 or § 503.

Section 501(c)(3) describes corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literacy, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in section (h)), and which does not participate in, or intervene in (including the publishing or distribution of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Section 7701(a)(40)(A) states that the term "Indian tribal government" refers to the governing body of any tribe, band, community, village, or group of Indians, or (if applicable) Alaska Natives, which is determined by the Secretary of the Treasury, after consultation with the Secretary of the Interior, to exercise governmental functions.

Section 7871(a) and § 305.7871-1 of the Income Tax Regulations provide that Indian tribal governments will be treated as states for certain enumerated federal tax purposes.

Section 7871(d) states that, for purposes of § 7871(a), a subdivision of an Indian tribal government shall be treated as a political subdivision of a state if (and only if) the Secretary of the Treasury determines (after consultation with the Secretary of the Interior) that the subdivision has been delegated the right to exercise one or more of the substantial governmental functions of the Indian tribal government.

Rev. Proc. 2002-64, 2002-2 C.B. 717, provides the most recent list of federally recognized tribal governments. In the situation described in this ruling, X is a federally recognized Indian tribal government.

Generally, federal income tax statutes do not tax Indian tribes. See Rev. Rul. 67-284, 1967-2 C.B. 55. An Indian tribe is not subject to federal income tax as an individual under § 1 or as a corporation under § 11. However, colleges and universities formed by Indian tribes are subject to § 511(a)(2)(B) (relating to the taxation of colleges and universities which are agencies or instrumentalities of governments or their political subdivisions) pursuant to § 7871(a)(5). Indian tribes also are subject to certain excise taxes.

Rev. Rul. 60-384, 1960-2 C.B. 172, provides circumstances under which a governmental agency is prohibited from qualifying as a § 501(c)(3) organization. A state or municipality itself will not qualify as an organization described in § 501(c)(3) since its purposes are clearly not exclusively those described in § 501(c)(3). Where a particular branch or department under whose jurisdiction the activity in question is being coordinated is an integral part of a state or municipal government, the provisions of § 501(c)(3) would also not be applicable.

Based on the above law and published guidance, X, an Indian tribal government, is not subject to federal income tax as an individual under § 1. Because an Indian tribal government is not subject to tax as an individual for § 1 purposes, it is not considered an individual under § 1361(b)(1)(B).

In addition, X, an Indian tribal government, does not qualify under the § 1362(c)(6) exception for certain exempt organizations described in § 501(c)(3) or § 401(a). X is not a § 401(a) organization because it is not a qualified pension, profit-sharing, or stock bonus plan. Furthermore, X is not a § 501(c)(3) organization because it is a government and its purposes are not exclusively those described in § 501(c)(3). Consequently, X is not an eligible S corporation shareholder, and Corporation cannot make an election to be an S corporation.

HOLDING

A federally recognized Indian tribal government is not an eligible S corporation shareholder for purposes of § 1361.

DRAFTING INFORMATION

The principal author of this revenue ruling is Laura C. Nash of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue ruling, contact Ms. Nash at (202) 622-3050 (not a toll free call).