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IRS Issues Proposed Guidance on Member Benefits

by Brian Deveau, National Practice Leader, and Jim Sharpe, Senior Manager, Tribal & Gaming Practice

For several years the IRS has been conducting audits of tribal governments and, in some cases, questioning whether certain benefits provided by tribes are tax-exempt governmental services or taxable benefits to the tribal member recipients. Finally, in December 2012, the Department of the Treasury released Notice 2012-75, Application of the General Welfare Exclusion to Indian Tribal Government Programs That Provide Benefits to Tribal Members. This notice introduces the IRS's proposed rules to determine what qualifies as a nontaxable benefit. The IRS is inviting public comment on the proposed rules until June 3, 2013.

General Welfare Exclusion Principles

Section 2.02 of the notice identifies three broad principles that must be met for benefits to be considered nontaxable. They must:

- Be made pursuant to a governmental program of the tribe

- Be made for the promotion of general welfare (based on individual need)
- Not represent compensation for services

These criteria could mean that payments to individuals that aren't part of a formal program established and approved by the governing body—or payments made without an individual "needs test"—may well be considered taxable to the recipients.

Benefits Where "Need Is Presumed"

Notice 2012-75 doesn't detail exactly what level of individual need will qualify, but it does include six criteria that, if met, will presume the benefits meet the needs test:

- The benefit is provided pursuant to a specific tribal government program.
- The program has specific written qualification guidelines.
- The benefit is available to any tribal member who meets the program guidelines.
- The benefit doesn't discriminate in favor of members of the governing body.
- The benefit isn't compensation for services.
- The benefit isn't lavish or extravagant.

In addition, the notice specifies certain benefits that would be presumed to meet the needs test, including:

Tribal Services Profile



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- Housing (rent, mortgage, or utility assistance or housing repairs and rehabilitation)
- Education (transportation, tuition, books and supplies, job counseling, and interview expenses, such as clothing or uniforms)
- Elder and disabled member assistance (meals, home care, certain transportation and travel, and housing adaptations, such as grab bars and ramps)
- Cultural and religious activities (expenses to attend a tribe's cultural, social, or community activities; visits to other culturally and historically significant Indian reservations; tribal culture, history, and traditions instruction costs; and funeral and burial expenses and related costs)
- Other circumstances (transportation from a reservation to public facilities, travel and other costs related to medical care or for victims of abuse, temporary relocation and shelter for displaced tribal residents, and the cost of nonprescription drugs)

Benefits presumed *not* to be compensation for services include nominal cash payments to "medicine men or women, shamans, or similar religious or spiritual officials" in recognition of their participation in cultural, religious, or social events.

Questions Remain

This guidance represents improved clarity from the existing tax code; however, there's much it doesn't answer. For example:

- What happens if the IRS disagrees with a tribe's assessment of "individual need"?
- What documentation must be retained to document individual need to withstand IRS audits?
- What qualifies as "written qualification guidelines"?
- What about traditional programs and benefits that aren't in writing?

- What constitutes a "lavish or extravagant" (and therefore taxable) benefit?
- What constitutes a "nominal" (and therefore nontaxable) payment to religious or spiritual officials?

What's Next?

It bears repeating that these rules are merely proposed at this point and aren't officially in effect. However, getting ahead of the curve and taking inventory of your tribe's benefit payments now could save a good deal of time, effort, and cost later. We also recommend that your tribe:

- Review the full text of the notice with legal counsel to gain a more thorough understanding of the proposed guidance
- Review existing general welfare programs in light of this new guidance to determine the impacts if the guidance is adopted
- Provide comments to the IRS (you can e-mail them to notice.comments@irs.counsel.treas.gov) prior to the deadline of June 3, 2013

Moss Adams LLP can help. Contact us for assistance in evaluating your benefit programs in light of the proposed guidance.