

INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

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CASE MIS No.: TAM-106419-00/CC:ITA:B5

Chief, Appeals Office

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification No:
Years Involved:
Date of Conference:

LEGEND:

Tribe:
Trust:
Trust Agreement:

A:
B:
C:
D:
E:
F:
G:
H:
I:
J:
K:
L:
M:
N:
O:
P:
Q:
R:
S:
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U:

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X:

Y:

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AA:

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HH:

II:

JJ:

KK:

Date 1:

Date 2:

Date 3:

ISSUE:

Whether A received gross income under § 61 of the Internal Revenue Code when the Tribe funded the Trust with payments for the benefit of A.

CONCLUSION:

A did not receive gross income when the Tribe funded the Trust.

FACTS:

X is a federally recognized Indian tribal government organized and operating under a Constitution approved by the Secretary of the Interior pursuant to the Indian Reorganization Act of 1934, ch. 576, § 16, 48 Stat. 987, codified as amended at 25 U.S.C. § 476 (1994). As provided in the Constitution, X's governing body is its B. The C of the Tribe performs such duties as may be authorized by the B. Among the enumerated powers of the B set forth in D of the Constitution are powers to

Congress enacted the Indian Gaming Regulatory Act, 25 U.S.C. 2701 (Act), on

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October 17, 1988. M of the Act provides that the purpose of the Act is to provide a statutory basis for the operation of gaming by Indian tribes as a means of promoting tribal economic development, self-sufficiency, and strong tribal governments, and to declare that the establishment of independent federal regulatory authority for gaming on Indian lands, and the establishment of a National Indian Gaming Commission, are necessary to meet congressional concerns regarding gaming and to protect such gaming as a means of generating tribal revenue.

Section 11(b)(3) of the Act provides that net revenues from any class II gaming activities conducted or licensed by any Indian tribe may be used to make per capita payments to members of the Indian tribe only if:

(A) the Indian tribe has prepared a plan to allocate revenues to uses authorized by section 11(b)(2)(B);

(B) the plan is approved by the Secretary of the Interior as adequate, particularly with respect to the uses described in clause (i) or (iii) of paragraph (2)(B);

(C) the interest of minors and other legally incompetent persons who are entitled to receive any of the per capita payments are protected and preserved and the per capita payments are disbursed to the parents or legal guardian of such minors or legal incompetents in such amounts as may be necessary for the health, education, or welfare, of the minor or other legally incompetent person under a plan approved by the Secretary and the governing body of the Indian tribe; and

(D) the per capita payments are subject to federal taxation and tribes notify members of such tax liability when payments are made. Under section 11(d), class III gaming activities are lawful on Indian lands if they meet the requirements of section 11(b).

On Date 1, the Tribe enacted the E. The E had two central purposes. First, as set forth in E, it

. Second, it established a plan for allocation of available monthly proceeds of the G of the Tribe, including L percent for per capita payments for adults (provided for in M) and N percent for the Children's Trust Fund (provided for in Q). The E was approved by the Area Director of the Q of the BIA, the designee of the Secretary of the Interior for approving the Tribe's revenue allocation plan under IGRA.

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M of the E provided that after certain deductions, up to H percent of the remaining available net proceeds of the Tribe's G may be paid to individuals listed on the I and to the minor children listed on the J when those minor children reach the age of K as provided in Q.¹

Q of the E, provided that N percent of the available monthly net proceeds of tribal G shall be divided equally among individual trust funds that shall be established by the C for the benefit of the minor children of persons identified in the E as entitled to be listed on the J and to receive these benefits. P provided that all such trust funds shall be placed at the best available rate in federally insured investments. P further provided that the trust instruments shall provide for distribution of R percent of the trust assets at age K, S percent of the trust assets at age T, and the remainder of the trust assets at age U.

F of the E provided that the list of persons on the I and the J and their descendants shall comprise the V list of persons entitled to receive payments and other benefits from the present and future G of the Tribe.

W of the E provided that except as otherwise provided in the E, the E may only be amended or rescinded by an affirmative

In X, the B enacted a comprehensive amendment (the "X Amendment") to supersede the E. The central purpose of the amendment was to

. There is no language comparable to F of the E in the X Amendment, and F is no longer part of tribal law.

¹ The individuals on the I and the J are listed in attachments to the E. A is listed on the J.

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The X Amendment (1) clarified that the E was intended to govern the allocation only of tribal gaming revenues, not other tribal revenues, and (2) retained the revenue allocation percentages set forth in the E, including the per capita payment program for adults (provided for in Y of the X Amendment) and the Children's Trust Fund (provided for in Z of the X Amendment). The X Amendment was approved by the Area Director of the Q of the BIA, under BIA Guidelines dated December 21, 1992.

On Date 2, the Tribe entered into the Trust Agreement with AA. The Trust Agreement was established pursuant to the E for payments made to the trusts after BB.² The Trust Agreement creates separate revocable trusts for each eligible minor. CC of the Trust Agreement provides that the C hereby transfers and assigns the assets described on the schedules attached (DD years of payments from EE to FF) to the trustee to constitute the original assets of each separate revocable trust created by this agreement and each such trust shall bear the name of the individual for whom it is created. CC further provides that each separate trust shall be administered pursuant to the provisions of this agreement for the primary benefit of the individual for whom it is named.

GG of the Trust Agreement provides, in part, that pursuant to Q of the E, N percent of the available monthly net proceeds of tribal G shall be divided equally among individual trust funds which shall be established by the C for the benefit of certain minors listed on the J and any subsequent descendants who are certified as qualified recipients.

HH provides that the C shall have the following powers with respect to each separate trust:

To amend any administrative provision of this agreement in whole or in part by a written instrument executed by the C and the then acting trustee;

To revoke any and all trusts created under this agreement by a written instrument executed by the C after such revocation is approved by a

Consistent with this power to revoke, the Tribe's audited financial statements have consistently included the assets held in the trusts among the cash and other assets belonging to the Tribe.

² The Tribe made payments from the Tribe's class II and III gaming activities to a separate AA investment account for DD years before establishing the trusts. The AA account was in the Tribe's name and the monies were not separated into separate minor accounts. After the Tribe established the trusts, it transferred the AA account to the trusts.

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II of the Trust Agreement provides, in part, that the separate trust for the primary benefit of the individual for whom it is named shall be administered as follows:

When the beneficiary attains the following ages, the following portions of the trust assets shall be distributed to the beneficiary: at age K, R percent of the then principal; at age T, S percent of the then principal; and at age U, the remaining assets of the trust.

If any trust assets remain at the beneficiary's death, the trust shall terminate and the remaining trust assets (including any accrued net income) shall be distributed to the beneficiary's estate.³

JJ of the Trust Agreement provides that the law of the Tribe and/or the State, except as altered by the Trust Agreement, shall govern the meaning and legal effect of the Trust Agreement and the administration of the trusts.

LAW AND ANALYSIS:

Section 61 of the Internal Revenue Code defines gross income as income from whatever source derived. Generally, a taxpayer using the cash receipts and disbursements method of accounting ("cash method") does not recognize gross income upon the receipt of property in the form of a promise to pay in the future. However, a cash method taxpayer is taxed when the taxpayer receives an "economic benefit" from a right to receive property in the future.

In Sproull v. Commissioner, 51 T.C. 244 (1951), aff'd per curiam, 194 F.2d 541 (6th Cir. 1952), the court held that the amount placed in trust to be paid out to the taxpayer in later years conferred an economic benefit on the petitioner in the year the trust was funded. In that case, the taxpayer, a corporation president, voluntarily decreased his compensation. In a later year, when the corporation was sound financially, a trust was set up by the board of directors for the benefit of the taxpayer. In determining that funding the trust conferred an economic benefit on the taxpayer in the year the trust was established, the court noted that the funds were placed in trust irrevocably for the taxpayer's sole benefit and that the taxpayer had to do nothing further to establish his right to it.

³ As permitted under HH, the C amended the Trust Agreement on Date 3 (Trust Amendment). The Trust Amendment provides that the C hereby revokes in its entirety KK of the Trust Agreement and substitutes and inserts in lieu thereof a new KK, which provides that if any trust assets remain at the beneficiary's death, the trust shall terminate and the remaining trust assets (including any accrued net income) shall revert to the Tribe. This amendment applies to all funds previously contributed to the trusts.

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The economic benefit doctrine has also been applied to require inclusion in income of prize winnings when they are irrevocably placed in a fund to be paid to the winner at a later date. See Pulsifer v. Commissioner, 64 T.C. 245 (1975); Anastasio v. Commissioner, 67 T.C. 814 (1977); Rev. Rul. 62-74, 1962-1 C.B. 68; Rev. Rul. 67-203, 1967-1 C.B. 105.

Rev. Rul. 83-25, 1983-1 C.B. 116, holds that a minor received the economic benefit of a trust when it was established by court order to receive damages awarded to the minor as a result of a personal injury suit. Under the terms of the trust, the trustee was authorized to distribute funds necessary for the health, education, support, or maintenance of the minor. The trust was not subject to revocation by the minor, but was subject to amendment, modification, or revocation by the court. The trust was to terminate upon the minor reaching the age of T, at which time the trust would distribute all of its property to him. If the minor died before reaching the age of T the trust property would pass to the minor's estate.

In the instant case, both the X Amendment to the E and the Trust Agreement impose various restrictions and conditions on A's ability to obtain the trust amounts. First, the X Amendment repealed former F of the E, which had provided that no person listed on the I or the J would ever be denied payments or benefits. Without this provision, nothing guarantees that the minors will ever receive payments from the trusts. Second, HH of the Trust Agreement specifically provides that the C has the power to revoke any and all trusts created under the Trust Agreement by a written instrument executed by the C after the revocation is approved by a

. Thus, the trusts are revocable trusts. Third, II of the Trust Agreement (as amended on Date 3) provides that if any trust assets remain at the beneficiary's death, the trust shall terminate and the remaining trust assets (including any accrued net income) shall revert to the Tribe.⁴ Finally, the Tribe's audited financial statements have consistently treated the assets held in the trusts as belonging to the Tribe.

On the other hand, these factors arguably are inconsistent with section 11(b)(3)(C) of the Act, which states that the interests of minors and other legally incompetent persons who are entitled to receive any of the per capita payments must be protected and preserved. It is unclear whether this broad language gives the minors any rights in excess of the contingent rights granted in the X Amendment and the Trust Agreement. However, we note that the X Amendment was specifically approved by the Area Director of the Q of the BIA. In addition, considering the language of the Act together with the specific provisions of the X Amendment and the Trust Agreement, it is

⁴ This fact distinguishes the Trust from the trust at issue in Rev. Rul. 83-25, which provided that the trust property would pass to the minor's estate if the minor died before receiving the trust property.

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clear that the Trust is a revocable trust and does not guarantee payments to the beneficiaries. Accordingly, A did not receive an economic benefit when Tribe funded the Trust with payments for the benefit of A.

A copy of this technical advice memorandum is to be given to A. Section 6110(k)(3) provides that it may not be used or cited as precedent.