

# ARIZONA DEPARTMENT OF REVENUE

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## **ARIZONA INDIVIDUAL INCOME TAX RULING ITR 96-4**

(Effective immediately and applicable to all open tax years)

### **This ruling supersedes Arizona Income Tax Ruling ITR 91-3**

This substantive policy statement is advisory only. A substantive policy statement does not include internal procedural documents that only affect the internal procedures of the agency and does not impose additional requirements or penalties on regulated parties or include confidential information or rules made in accordance with the Arizona administrative procedure act. If you believe that this substantive policy statement does impose additional requirements or penalties on regulated parties you may petition the agency under Arizona Revised Statutes § 41-1033 for a review of the statement.

#### **ISSUE:**

Income Taxation of Indians and Spouses.

#### **LEGAL REFERENCES:**

There are no specific statutory references relative to the imposition of the Arizona Income Tax upon Indians. This ruling is based on the decisions in the following court cases: McClanahan v. State Tax Commission of Arizona, 411 U.S. 164, 93 S. Ct. 1257 (1973); Warren Trading Post Company v. Arizona State Tax Commission, 380 U.S. 685, 85 S. Ct. 1242 (1965); Central Machinery Company v. Arizona State Tax Commission, 448 U.S. 160, 100 S. Ct. 2592 (1980); State of Washington v. Confederated Tribes of the Colville Reservation, 447 U.S. 134, 100 S. Ct. 2069 (1980); Ramah Navajo School Board, Inc. v. Bureau of Revenue of New Mexico, 458 U.S. 832, 102 S. Ct. 3394 (1982); Oklahoma Tax Commission v. Sac and Fox Nation, 113 S. Ct. 1985 (1993); Oklahoma Tax Commission v. Chickasaw Nation, 115 S. Ct. 2214 (1995).

#### **DISCUSSION:**

The above cited opinions imply that an Indian who lives and works on a reservation and who is an affiliated member of the tribe for whose benefit that reservation was established is not liable for state income taxes. These opinions do not preclude the department from imposing a state income tax on the income of a non-affiliated Indian (one who, although being an enrolled member of one tribe, is not affiliated with the tribe of the reservation where he or she is employed and receiving income).

The proper application of the State Income Tax Act with regard to a non-affiliated Indian or non-Indian who is the spouse of an affiliated Indian living and working on the reservation remains to be determined by the courts.

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### **CONCLUSION AND RULING:**

To facilitate administration of the income tax laws relating to the taxation of income earned on an Indian reservation, the department has adopted the following position:

1. In general, an Indian is subject to the Arizona state income tax unless the Indian (1) is living and working on the reservation, and (2) is deriving income from reservation sources only, and (3) is an affiliated member of the tribe for which that reservation was established. Any income derived from nonreservation sources by an Indian is subject to the Arizona state income tax. Arizona will not impose tax on an Indian's income derived from reservation sources if the Indian lives on the reservation and the Indian is an affiliated member of the tribe for whose benefit that reservation was established.
2. Income of a non-affiliated Indian or a non-Indian derived from reservation or nonreservation sources while working and living on or off a reservation is subject to tax in the same manner as all other Arizona residents.
3. Income of a non-Indian spouse or a non-affiliated Indian spouse of an affiliated Indian is subject to the Arizona state income tax.
4. Generally, for a married couple comprised of an affiliated Indian and a non-Indian or non-affiliated Indian, Arizona community property laws are to be applied as follows:
  - a. If the couple files a joint Arizona income tax return, to the extent included in Arizona gross income, the following income shall be subtracted in determining Arizona adjusted gross income:
    - (1) the income earned by the affiliated Indian from reservation sources while living on the reservation;and
    - (2) one-half of the non-Indian spouse's or non-affiliated Indian spouse's community income earned from reservation sources while living on the reservation.
  - b. If the couple chooses to file married filing separate returns, to the extent included in each spouse's respective Arizona gross income, the following income shall be subtracted in determining Arizona adjusted gross income:
    - (1) for the affiliated Indian, the amount of reservation source income he or she earned while living and working on the reservation plus the amount of reservation source community income earned by his or her spouse while living on the reservation.
    - (2) for the non-affiliated Indian or non-Indian, the amount of reservation source community income earned by the affiliated Indian spouse while living on the reservation.
  - c. Full deductions and dependent exemptions are allowed as provided in the Income Tax Code.

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5. For purposes of this ruling, an affiliated Indian includes any Indian who has been adopted into the tribe and who has attained full and unrestricted membership privileges in that tribe. In order for an adopted Indian to qualify for the income tax exemption, the Indian must provide acceptable proof of tribal membership.

Harold Scott, Director

Signed: May 29, 1996

### Explanatory Notice

The purpose of a tax ruling is to provide interpretive guidance to the general public and to department personnel. A tax ruling is intended to encompass issues of law which are not adequately covered in statute, case law or administrative rules. A tax ruling is a position statement which provides interpretation, details or supplementary information concerning the application of the law. Relevant statute, case law, or administrative rules, as well as a subsequent ruling, may modify or negate any or all of the provisions of any tax ruling. See GTP 96-1 for more detailed information regarding documents issued by the Department of Revenue.