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INCOME TAXATION OF DISTRIBUTIONS BY ALASKA NATIVE CORPORATIONS: AN AMBIGUITY IN NEED OF CLARIFICATION

Meade Emory and Robert A. Warden*

Abstract: In 1971, Congress passed the Alaska Native Claims Settlement Act ("ANCSA") to provide compensation for extinguishing Native land claims in Alaska. ANCSA created a system of village corporations that received money and land as compensation, and are to distribute the compensation to shareholders. The Internal Revenue Service ("IRS"), despite legislative history to the contrary, is now asserting that corporate tax principles apply to the distributions because of ambiguous language contained in ANCSA. This assertion makes distributions to shareholders taxable as dividends to the extent of the corporations' accumulated and current earnings and profits. The IRS stance will result in excessive taxation of the shareholders due to the unique manner in which ANCSA is set up, and due to poorer economic values of the Natives' land bases. The authors argue that Congress should amend ANCSA to relieve the corporations and shareholders of the unintended taxation. They examine ANCSA and its legislative history, and contrast the IRS's letter rulings to show how the IRS interpretation is contrary to the legislative intent. Finally, the authors propose two alternative amendments that would clarify the otherwise coherent ANCSA policy against imposing an income tax on compensation for extinguishing aboriginal land claims, and assure that individual Natives receive the full measure of compensation that Congress intended to convey.

The Alaska Native Claims Settlement Act ("ANCSA"),¹ the 1971 legislation by which Congress settled the aboriginal land claims of Alaska Natives, created a system of corporations that today encounter an inappropriate application of corporate income tax law upon distributions² to shareholders with respect to stock. On behalf of individual Alaska Natives, these corporations have received money and land as compensation for the extinguishment of land claims. ANCSA's legislative history recognizes the general principle that compensation for extinguishment of Alaska Native land claims does not constitute taxable income. In accordance with this principle, ANCSA allows the

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². In this Article, the term "distribution" refers to a distribution with respect to a corporation's stock. See I.R.C. § 301(a) (1982).
money portion of the compensation to pass through the Alaska Native corporations to their shareholders tax free. However, the statutory language does not expressly preclude income tax on distributions by an Alaska Native corporation insofar as such distributions reflect the value of the land and natural resources that comprise the bulk of the compensation package. Based on the current statutory language, the Internal Revenue Service ("IRS") has taken the position in letter rulings that such distributions are subject to ordinary corporate tax law. Under this view, such distributions clearly are taxable as dividends to the extent of the corporation's current or accumulated earnings and profits. Because this result is inconsistent with the apparent intent of the 1971 legislation, an amendment is necessary to clarify ANCSA's compensatory scheme.

The thesis of this Article is that Congress should amend ANCSA to provide that a distribution by an Alaska Native corporation is not taxable income to individual Native shareholders to the extent the distribution reflects the value of land or interests in land which the corporation has received pursuant to ANCSA. Section I demonstrates that the current absence of such a provision creates uncertainty in an otherwise coherent ANCSA policy against the imposition of an income tax on compensation for the extinguishment of aboriginal land claims. Section II explains that, under the current IRS interpretation of ANCSA, the shareholders of certain Alaska Native corporations may be subject to income tax on distributions of such compensation by the Native corporations in which they hold stock. Section III proposes two alternative legislative solutions to this problem.

I. THE CENTRAL PRINCIPLE: NO TAX ON COMPENSATION

The central principle of income taxation under ANCSA is that the property the Natives have received as compensation for the extinguishment of aboriginal land claims does not constitute taxable income. In accordance with this principle, ANCSA shields Native corporations from income tax on receipt of property under ANCSA, and also shields individual Natives from income tax on certain cash

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3. Section II of this Article discusses the IRS position in detail.

4. In this Article, references to land that a Native corporation has received pursuant to ANCSA generally include any "interest" in land a Native corporation has received. Although ANCSA does not define "interest" in land, the term appears to include any estate in land less than the entire fee, such as the surface estate or subsurface estate, and any extractable resource, such as timber or oil.
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distributions from their corporations. However, ANCSA does not unequivocally protect individual Natives from income tax on corporate distributions of land or proceeds from the sale of the land. This gap in the protection from income tax is enormously significant to the Natives, for the Natives derive most of their compensation from the land they receive, particularly from the sale of the land or the natural resources the land contains.

A. Form of the Compensation

The purpose of ANCSA was to effect an equitable settlement of the aboriginal land claims held by Alaska Natives. The settlement package consisted of land and money. Congress did not attempt to place a precise value on the aboriginal land claims that ANCSA extinguished but accepted as appropriate the settlement package that the House Committee deemed “fair to the Natives, fair to the State of Alaska, and fair to all of the people of the United States, in light of present day conditions.” ANCSA extinguished all aboriginal land claims held by Alaska Natives as of December 18, 1971.

Unlike any previous settlement with Native Americans, ANCSA required Alaska Natives to form corporations through which to receive their compensation. All compensation pursuant to ANCSA was to pass initially to newly formed Native corporations rather than directly to individuals or tribal units. Prior settlements with native Americans had been effected without the use of intermediary corporations. In retrospect, many people have questioned whether the “for-profit corporation” is the “only appropriate form of legal entity to implement the [Alaska Native claims] settlement in all regions and all

5. Subsection B of this Section describes ANCSA tax provisions in detail.
6. As Subsection A of this Section explains, the settlement package included $962,500,000 and 40,000,000 acres of land. Simple algebra indicates that the dollar value of the land is much greater than the cash portion of the settlement package if one assumes any reasonable per acre value for the land. The per acre value of the land is quite substantial insofar as the land contains marketable natural resources.
8. Id. at 2195. As set forth in the House Report, the relevant present day conditions included the “extreme poverty” and “underprivileged status” of the Natives. Id. at 2195–96.
9. 43 U.S.C. § 1603(b), (c) (1982); see United States v. Atlantic Richfield Co., 612 F.2d 1132, 1134 (9th Cir.), cert. denied, 449 U.S. 888 (1980). Under section 5(a) of ANCSA, the roll of Natives eligible for compensation includes “all Natives who were born on or before, and who are living on, December 18, 1971.” 43 U.S.C. § 1604(a) (1982).
Moreover, the 1988 amendments to ANCSA provide for an alternative form of organization, specifically a State-Chartered Settlement Trust. In 1971, however, incorporation was essentially mandatory. This requirement of incorporation reflected an expectation that Native enterprises eventually might assimilate into the non-Native business mainstream.

Native corporations are unique. Unlike ordinary corporations, Native corporations are not voluntary aggregations of capital. They are not voluntary because the Natives, who own the corporations, had no opportunity to take their compensation in any other form and generally do not have the option to sell their stock. Moreover, Native corporations are not aggregations of capital in the normal sense because the primary assets of the Native corporations originally emanated from the government. In this light, Native corporations are intermediaries between the government and the Natives. They act as conduits for the transfer of compensation to the individual Natives.

Under section 7(h)(1) of ANCSA, all stock of a Native corporation must contain a restriction on alienation effective for twenty years after December 18, 1971. The 1988 amendments extended such restrictions indefinitely with respect to most Native corporations, subject to an affirmative decision by a particular corporation to terminate the restriction on alienation of its stock after December 18, 1991.

ANCSA contemplated two types of Native corporations: regional corporations and village corporations. Under section 7 of ANCSA, the Native residents of twelve geographic regions formed twelve regional corporations, while Natives outside these twelve regions combined to form a thirteenth regional corporation. Within the twelve geographic regions, ANCSA identified 215 Native villages by name.

Under section 8 of ANCSA, the Native residents of each of these

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15. 43 U.S.C. § 1606(a), (c) (1982).
16. Section 11(b)(1) of ANCSA contains a list of 205 Native villages. 43 U.S.C. § 1610(b)(1) (1982). Section 16(a) lists another nine. Id. § 1615(a). In addition, section 16(d) provides specially for the village of Klukwan. Id. § 1615(d). Other Native corporations that may receive ANCSA settlement property include four “urban corporations,” see 16 U.S.C. § 3102(9) (1982), as contemplated by section 14(h)(3), and an indeterminate number of incorporated Native groups, as contemplated by section 14(h)(2). 43 U.S.C. § 1613(h)(3) (1982); id. § 1613(h)(2).
Native villages formed their own village corporation. Pursuant to the terms of the settlement, each of the regional and village corporations would receive distributions of money from the Alaska Native Fund and would select tracts of land for conveyance by the Secretary of the Interior.

1. Alaska Native Fund

ANCSA required the United States Treasury to establish the Alaska Native Fund, an account in the Treasury for the deposit of money subject to distribution to regional corporations and village corporations under ANCSA. Under section 6 of ANCSA, this money included $462,500,000 from the general fund of the Treasury, as well as $500,000,000 from the State of Alaska in mineral royalties. Section 6 contemplated that the Treasury and the State of Alaska would pay into the Alaska Native Fund over a period of years (at least through 1981), and that each regional corporation would receive quarterly distributions from the Alaska Native Fund, on the basis of total Native enrollment in its region, as long as the fund lasted.

By the express terms of ANCSA, the regional corporations served as conduits for the distribution of money from the Alaska Native Fund to village corporations and individual shareholders. ANCSA required each regional corporation to distribute part of its revenue from the Alaska Native Fund as well as part of all other net income. Section 7(j) of ANCSA specified that for the first five years after December 18, 1971, each regional corporation for a geographic region would distribute at least 10% of this money to its shareholders and at least 45% to village corporations within the region and to shareholders not members of any village. After five years each regional corporation for a geographic region would distribute 50% of this money to village corporations in the region and to shareholders not members of any village. Moreover, the thirteenth regional corporation would distribute 50% of this money to shareholders.

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18. Id. § 1605.
19. Section 6 of ANCSA set forth a schedule for the Treasury's contribution to the Alaska Native Fund. Id. The schedule extends through 1981. Section 9 of ANCSA required the State of Alaska to contribute mineral royalties as long as necessary to reach a total contribution of $500,000,000. Id. § 1608(d).
20. Section 6(c) specified that the U.S. Treasury would distribute all money in the Alaska Native Fund to the regional corporations on a quarterly basis, except for certain reserve requirements. Id. § 1605(c). As the schedule for the Treasury's contributions to the Fund extended through 1981, distributions to the regional corporations must continue at least until then.
21. Id. § 1606(j).
2. Land Selection

The land available for selection by Native corporations under ANCSA consisted of certain federal properties in those Alaska townships that contain Native villages. Pursuant to section 14 of ANCSA, the Secretary of the Interior was to convey to each Native corporation a patent to the property that the corporation selected. The total amount of land that Native corporations are to receive under ANCSA is 40,000,000 acres. Village corporations are to receive the surface estate to 22,000,000 acres, while regional corporations are to receive the surface estate to most of the balance of the total acreage, as well as virtually all subsurface estates. Section 14(c) required that Native corporations, upon receipt of conveyances of land from the Secretary of the Interior, immediately would reconvey portions of such land to municipalities, individuals, and other current occupants. The total number of acres the Native corporations are to receive under ANCSA reflects an estimate of the acreage necessary to generate economic development. However, many unforeseen delays have occurred in the land selection process. As of early 1988, the Bureau of Land Management, which administers the process for the Secretary of the Interior, had not yet conveyed all of the land.

The value of the 40,000,000 acres of land was significantly greater than the dollar amount of the Alaska Native Fund. Congress anticipated that the Natives would select land with economic potential, particularly extractable natural resources. For the village corporations,

23. Under section 12(b) of ANCSA, the village corporations were to receive the surface estate to a full 22,000,000 acres, whether or not they actually selected this much land. Id. § 1611(b) (1982). Under section 14(f), the regional corporations were to receive the subsurface estate to all of this land, with certain exceptions for land reserved for defense purposes or as a wildlife refuge. Id. § 1613(f). Under section 12(c), the regional corporations were to receive 16,000,000 acres, which would include subsurface estates with the same exceptions as above. Id. § 1611(c). Under section 14(h), there were another 2,000,000 acres available for miscellaneous groups. Id. § 1613(h). The regional corporations were to receive the subsurface estates to this land, with certain restrictions, and the surface estate to any portion of the land that did not go to another group.
24. Id. § 1613(c).
27. Id. at 20, reprinted in 1987 U.S. CODE CONG. & ADMIN. NEWS at 3270.
which received only the surface estate of the land they selected, timber was ordinarily the most significant resource available.

The volatility of the timber market, together with the delays in the transfer of timber property to many Native corporations, resulted in timber sale proceeds to the corporations that were substantially less than what Congress presumably had envisioned. After 1980, when the Bureau of Land Management transferred most of the timber property that Native corporations had selected, timber prices declined drastically. Despite the decline in the market, the Native corporations sold timber periodically to meet the income needs of their shareholders—many of whom were poor in 1971 and have remained so. Native corporations were unable to take advantage of the market highs which Alaska timber had previously enjoyed.

For purposes of this Article, the significance of the decline in timber prices after 1980 is that Native corporations generally have lost money on sales of ANSCA property and can expect similar losses on any such sales in the foreseeable future. The pool of sale proceeds potentially available for distribution by any Native corporation is less than the original value of the land and timber the Native corporation has sold. If a corporation were to sell all of its land and timber anytime in the near future, the corporation would incur a large loss for income tax purposes. Therefore, the pool of sale proceeds available for distribution by a Native corporation does not include any net gain that constituted taxable income at the corporate level. In other words, the sale proceeds reflect only corpus of the settlement package, not income.

B. Application of the Central Principle

Section 21 of ANCSA, which dealt with the tax aspects of ANCSA transfers, implicitly established the central principle that compensation for extinguishment of aboriginal land claims is not taxable. In the section-by-section analysis of the Senate bill, the Senate Committee expressly recognized "the general principle that the resources hereby made available represent compensation for the extinguishment of Native land claims by the operation of this Act, and that in accordance with general principles of taxation such compensation does not constitute taxable income."

The central principle of section 21 is derived from the characterization of the settlement package as compensation for the aboriginal land claims. In effect, Congress treated the settlement package as personal injury damages, which generally are not taxable.\textsuperscript{31} For tax law purposes, a personal injury is not necessarily a physical injury. For example, defamation may constitute a personal injury for tax law purposes if under applicable local law the tort of defamation relates primarily to the personal interest in one’s good name.\textsuperscript{32} Insofar as defamation is a personal injury, damages for defamation are nontaxable in their entirety, although the measure of such damages is usually in pecuniary terms. The extinguishment of aboriginal land claims of Alaska Natives under ANCSA is a personal loss because the land claims are an integral part of Alaska Native culture. The extinguishment of aboriginal land claims ultimately threatens the survival of the culture through which the land claims arose. The value of culture is clearly more personal than pecuniary; this is especially true of an aboriginal culture. Hence the treatment of the ANCSA settlement package as personal injury damages reflects an appreciation of the land’s importance as an aspect of Native culture.

A corollary to the central principle of section 21 was that any income that a Native corporation or Native individual may earn on the money and land received pursuant to ANCSA would be fully taxable, as such income does not constitute “compensation” for the extinguishment of land claims. In other words, ANCSA did not create a general tax exemption for Native corporations or Native individuals but only recognized that the value of the settlement package at the time of receipt was not subject to taxation.

1. Receipt of Revenue from Alaska Native Fund

In accordance with the central principle that compensation for aboriginal land claims is not taxable, section 21(a) of ANCSA\textsuperscript{33} provides that “revenues” from the Alaska Native Fund are not subject to any form of taxation, either upon receipt by a regional corporation or village corporation or by individual Natives through “dividend distri-

\textsuperscript{31} T.R.C. § 104 (1982); see also Roemer v. Commissioner, 716 F.2d 693, 698-700 (9th Cir. 1983); B. BITTKER, FEDERAL TAXATION OF INCOME, ESTATES, AND GIFTS 13.1.4 (1981).

\textsuperscript{32} Roemer, 716 F.2d at 698-700. However, the IRS does not follow Roemer and maintains that defamation is a personal injury only insofar that damages reflect injury to personal interest rather than injury to business or professional interests. Rev. Rul. 85-143. 1985-2 C.B. 55-56.

\textsuperscript{33} 43 U.S.C. § 1620(a) (1982).
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...butions or in any other manner." 34 Under section 21(a), a regional corporation was not subject to income tax on receipt of quarterly distributions from the Alaska Native Fund, and village corporations and regional corporation shareholders were not subject to income tax on receipt of the distributions that ANCSA required from the regional corporations. Moreover, voluntary distributions of Alaska Native Fund money, by either regional corporations or village corporations, are not taxable to distributee shareholders.

Section 21(a) also specifies that the exemption from income tax does not apply to income from investment of Alaska Native Fund money. Accordingly, investment income is taxable both at the corporate level and at the shareholder level. As a matter of theory, this caveat is uncontroversial, because income from the investment of Alaska Native Fund money does not constitute "compensation" for land claims. 35 However, practical application of this aspect of section 21(a) is problematic in the context of corporate distributions because dollars are fungible. In other words, a particular distribution arguably might consist of virtually any relative proportions of corpus and income. Originally, there seems to have been some sentiment that a Native corporation should establish a special account for Alaska Native Fund money that the corporation planned to distribute, so that the corporation actually could trace the source of a distribution to the Alaska Native Fund. 36

In 1988, Congress amended section 21(a) to clarify that the tax exemption for revenue from the Alaska Native Fund does not require segregation of such revenue into a separate account. 37 It appears that

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34. Presumably, the term "revenues" means the corporation's initial receipts from the Alaska Native Fund. Under the express language of section 21(a), any income a corporation or individual may earn on money received from the Alaska Native Fund is fully subject to taxation. 43 U.S.C. § 1620(a) (1982). Pursuant to an unpublished IRS letter ruling dated February 2, 1977, any income on the money prior to distribution from the Alaska Native Fund is not taxable to the Natives but is, rather, treated as a nontaxable corpus amount. In particular, the ruling states: "Interest income earned upon Fund money during the period before distribution to the Regional Corporation is not subject to federal income tax upon receipt by the Regional Corporation." Unpublished Priv. Ltr. Rul., Feb. 2, 1977, at II-15 (copy on file with Washington Law Review).

35. There is no bar to income tax on interest or income derived from a personal injury award. I.R.C. § 104 (1982).

36. See, e.g., Priv. Ltr. Rul. 81-38-123 (June 26, 1981). In this private letter ruling, the taxpayer, a village corporation, placed revenues from the Alaska Native Fund in a special account designated for subsequent distribution. With respect to these revenues, the IRS ruled that the subsequent distributions were not taxable to shareholders. However, the IRS did not purport to require segregation of revenues from the Alaska Native Fund.

37. Pub. L. No. 100-241, § 12(b), 101 Stat. 1788, 1810 (1988). This amendment added the parenthetical that applies the subsection's tax shield to dividend distributions: "(even if the
the 1988 amendment to section 21(a) allows a Native corporation to characterize any cash distribution as a distribution of revenues from the Alaska Native Fund. Thus, a corporation can insulate its shareholders from income tax on any distributions, until the corporation has distributed cash equal to the corporation's share of the Alaska Native Fund.

In effect, section 21(a) creates an exception to the rule of corporate tax law that every corporate distribution is a distribution from earnings and profits to the extent the corporation has any.\(^3\) Even if a Native corporation has positive earnings and profits, section 21(a) allows the Native corporation to treat its distributions to shareholders as distributions of money from the Alaska Native Fund, until such distributions exhaust the corporation's share of the Alaska Native Fund. Thus, a Native corporation's share of the Alaska Native Fund is singularly available for distributions to shareholders, apart from and without regard to earnings and profits.

The availability of Alaska Native Fund revenues for distribution outside the ordinary earnings and profits framework reflects a recognition of the unique status of Native corporations. When a Native corporation distributes such money to shareholders, the Native corporation serves as a conduit for the transfer of compensation from the government to the individual Natives. The distribution is quite different from an ordinary dividend or even a return of capital. It is a compensatory award. The money does not represent an investment by the Natives or a return on investment, for the money has never before passed through the hands of the individual Natives. Although the individual Natives receive their compensation through corporations, the ultimate distribution of cash retains the compensatory character of the Alaska Native Fund and is not subject to any inconsistent characterization under corporate tax law.

2. Receipt of Stock in Alaska Native Corporations

Section 21(b) of ANCSA\(^3\) provides that the receipt of stock in any regional corporation or village corporation by an individual Native is not subject to any form of taxation. Under this provision, the individual Natives did not pay income tax on their initial receipt of the stock
that represents each individual's interest in the settlement package of money and land.

Section 21(b) does not address the amount of each individual's basis in his or her stock. In accordance with IRS views, however, this Article treats the aggregate basis in a Native corporation's stock as equal to the corporation's receipts from the Alaska Native Fund plus the corporation's basis in the land which the corporation has received pursuant to ANCSA, reduced by the amount of any nontaxable distributions.\textsuperscript{40}

### 3. Receipt of Land or Interests in Land

Section 21(c) of ANCSA\textsuperscript{41} provides that the receipt of land or any interest in land "pursuant to this chapter"—i.e., pursuant to ANCSA—"shall not be subject to any form of Federal, State or local taxation." Moreover, section 21(c) specifies that a recipient's basis in such land or interest in land is equal to the value of the land or interest at the time of receipt. In 1980, Congress amended section 21(c) to provide that a recipient's basis in land with an extractable resource such as timber or a mineral deposit is equal to the greater of the value of the land at the time of receipt or the value of the land at the time of first commercial development.\textsuperscript{42}

Under section 21(c), any receipt of land or interests in land is not subject to income tax if the receipt of such land or interests was "pur-

\textsuperscript{40} On February 2, 1977, the IRS issued a private letter ruling to several Native corporations on certain basic tax issues under ANCSA. Although this ruling was never published, the IRS used this ruling to announce its position not only on the issues the applying corporations had raised but also on other matters that the IRS considered significant. In this ruling, the IRS stated that the computation of basis for the stock of Native corporations is as follows:

3. The basis of the stock of a Regional Corporation in the hands of its Native shareholders is equal to the cash transfers out of the Fund and the fair market value of lands received by and titled in the Regional Corporation. Basis of stock will be adjusted at the time of each cash receipt by a Regional Corporation from the Fund and each disbursement by a Regional Corporation of cash originally from the Fund to the Village Corporations or to the stockholders of a Regional Corporation. Section 358 of the Code.

4. Basis of stock of the Village Corporations in the hands of its Native shareholders is equal to the total of Fund receipts by the respective Village Corporation from the Regional Corporation and the fair market value of the surface lands titled in the Village Corporations. Basis of stock will be adjusted at the time of each cash receipt originally from the Fund to the Village Corporation, and each disbursement by the Village Corporation of cash originally from the Fund.


\textsuperscript{41} 43 U.S.C. § 1620(c) (1982).

\textsuperscript{42} Pub. L. No. 96-487, § 1408, 94 Stat. 2371, 2495-96 (1980). At the same time, Congress defined the time of receipt to mean the time of the conveyance by the Secretary of the Interior, whether by interim conveyance or patent.
suant” to ANCSA. Unquestionably, Native corporations received land “pursuant” to ANCSA when they accepted patents or interim conveyances from the Bureau of Land Management through ANCSA’s land selection process. Furthermore, occupants who received immediate reconveyances of their residences from Native corporations in accordance with express requirements of ANCSA clearly received land “pursuant” to ANCSA. As ANCSA does not expressly contemplate distributions of land or interests in land to shareholders, however, such distributions are not “pursuant” to ANCSA in the strictest sense. Certain Native corporations have raised the argument that such distributions are “pursuant” to ANCSA in a broader sense, but the argument has failed to persuade the IRS.

The new subsection (j) did not resolve the general issue of tax treatment of distributions of land or interests in land a Native corporation has received pursuant to ANCSA. First, this provision contained substantial restrictions under which an ordinary distribution with respect to stock would fail to qualify for nontaxable treatment. In other words, a distribution without any attempt to satisfy the special conditions of subsection (j) remains taxable. Second, the new subsection did not specifically contemplate general application to distributions with respect to stock. Although the internal politics of a village corporation might require that any distribution to shareholders take the form of a distribution with respect to stock, a village corporation conceivably might distribute homesites on an entirely different basis. For example, a village corporation might adopt a policy to distribute homesites only to those shareholders who satisfy a test of need or to distribute homesites so as to promote settlement in a particular area where some individuals would not choose to live. A village corporation might well decide to distribute homesites only to shareholders who will use the land as such, so that shareholders who already have a homesite superior to that which they might receive from the corporation would not participate.

Originally, subsection (j) did not apply to regional corporations, but this limitation was eliminated by the 1988 amendment. See Pub. L. No. 100-241, § 12(b), 101 Stat. 1788, 1810 (1988).

In particular, certain Native individuals have argued that such dividend distributions are nonetheless “pursuant” to ANCSA insofar as they are consistent with ANCSA’s broad compensatory design. Under this argument, the receipt of land “pursuant” to ANCSA is simply
As set forth in the introduction, the basic thesis of this Article is that ANCSA should provide for nontaxable corporate distributions of ANCSA land or resources, or cash equivalents. In essence, this Article propounds the argument that the tax treatment of the land and resources a Native corporation has received from the Bureau of Land Management should conform to the tax treatment of money the corporation has received from the Alaska Native Fund. Under the proposed regime, a Native corporation could distribute amounts that reflect the value of the land or resources, apart from and without regard to earnings and profits, and the shareholders would receive these amounts as nontaxable compensation. Section 21(c) in its present form does not unambiguously achieve such a result. As described in Section I.C of this Article, however, imposition of ordinary corporate tax rules is inconsistent with the compensatory character of ANCSA property, which includes both the Alaska Native Fund and the land and resources. Section II of this Article discusses the IRS's application of ordinary corporate tax rules to distributions of proceeds from the sale of ANCSA land or resources. Under these rules, the IRS treats such distributions as distributions out of earnings and profits to the extent a Native corporation may have positive earnings and profits. Section II also describes the significant problems of the IRS approach and details the need for a legislative response.

Although section 21(d)(1) might appear to resolve the tax treatment of distributions of proceeds from the sale of ANCSA land or resources, the provision merely heightens ambiguity. Under section 21(d)(1) of ANCSA, all “rents, royalties, profits, and other revenues or proceeds” from the land or interests in land that the Native corporations have received pursuant to ANCSA are taxable “to the same extent as such revenues or proceeds are taxable when received by a non-Native individual or corporation.” This provision clearly contemplates income taxation of a corporation’s return from the exploitation of land or resources as well as income taxation on any gain realized by a corporation on the sale of any such land or resources. As the basis of any such land or resources would be the fair market value at the time of receipt (or, after the 1980 amendment, the higher of the

the receipt of land which originates from the Secretary of the Interior and which, to the recipient, constitutes compensation for the extinguishment of land claims. In support of this position, the Natives have argued that section 21(c) of ANCSA provides that the "receipt of land or any interest therein" shall not be subject to "any form" of federal, state, or local taxation. 43 U.S.C. § 1620(c) (1982). According to the Natives, this language could be construed as including in-kind distributions of land or interests in land or sale proceeds.

value at the time of receipt or the value at the time of first commercial
development), gain will reflect only appreciation of the land that has
occurred after receipt by the Native corporation.

However, the proper application of the quoted language from sec-
tion 21(d)(1) is uncertain with regard to distributions of proceeds from
the sale of land or interests in land that a Native corporation has
received pursuant to ANCSA. The problem is whether this language
means that distributions of proceeds from the sale of ANCSA prop-
erty are subject to the general principles applicable to distributions to
shareholders, i.e., that distributions of such proceeds are taxable to the
extent of the corporation’s earnings and profits. Arguably, the refer-
cenced language from section 21(d)(1) applies only to proceeds that—
like rent, royalties or profits—constitute income. In other words, the
reference to “other revenues or proceeds” may denote forms of income
other than rents, royalties, or profits, but not amounts that are not
income to the corporation, such as the amounts attributable to the
recovery of the Native corporation’s basis. The doctrine of *ejusdem
generis* supports this interpretation. Under this interpretation, dis-
tribution of sale proceeds less than or equal to the corporation’s basis
would not necessarily give rise to taxation at the shareholder level.

C. Conflict Between General Corporate Tax Rules and the Central
Principle of ANCSA

The absence of any language in ANCSA that addresses the tax con-
sequences of a distribution of land, or proceeds from the sale of the
land, is a significant gap in the otherwise coherent ANCSA policy
against taxation on compensation for land claims. To the extent that
the absence of any such language results in the imposition of income
tax on amounts that represent the value of the land and natural
resources the Natives received pursuant to ANCSA, current law is
inconsistent with the general principle of ANCSA that compensation
for aboriginal land claims is not taxable.

There is a fundamental ambiguity in ANCSA with regard to
whether the actual compensation to the individual Natives is the
money and land, or merely stock ownership in the Native corporations

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48. The doctrine of *ejusdem generis* is a common law rule of statutory construction. Briefly,
this doctrine provides that:

Where general words follow an enumeration of persons or things, by words of a particular
and specific meaning, such general words are not to be construed in their widest extent, but
are to be held as applying only to persons or things of the same general kind or class as those
specifically mentioned.

that own the money and land. The individual Natives appear to have a direct entitlement to the money in the Alaska Native Fund, albeit through the Native corporations as conduits, because the individual Natives can receive nontaxable corporate distributions of this money. However, the entitlement of the individual Natives to the 40,000,000 acres of settlement land is unclear due to the absence of an express provision permitting nontaxable distributions of land or proceeds from the sale of land. The absence of such a provision tends to impound the settlement land at the corporate level, beyond the reach of the individual Natives.

If the individual Natives have a direct entitlement to the entire settlement package, then they should have the right to receive nontaxable distributions of both the money and the value of the land (but not income or appreciation realized on the property while in the possession of Native corporations). Income and appreciation should not be available for nontaxable distributions because these items are not "compensation." In other words, the money and the land constitute compensation only to the extent of the value Congress intended the Natives to receive directly from the United States Treasury or the Bureau of Land Management. With respect to the money, the value that constitutes compensation is simply the dollar amount the Native corporations receive from the Alaska Native Fund. With respect to land, the amount that constitutes compensation is the basis that section 21(c), as amended, assigns to such land.

It is not possible in this Article to resolve the ambiguity as to whether the individual Natives have a direct entitlement to the entire settlement package. There is ample reason, however, to doubt that Congress specifically intended the Native corporations to function as barriers between the individual Natives and the land portion of the settlement package.

First, Congress explicitly presented the land portion of the ANCSA settlement package as a conveyance to "the Natives" themselves. The aboriginal land claims that Congress extinguished through ANCSA had been the property of individual Natives. Hence the entitlement to compensation resided with the individual Natives as well. There is no statement in the legislative history to the effect that distributions of land, or proceeds from the sale of the land, are subject to taxation at the shareholder level.

Second, the Native corporations or similar entities were apparently interposed as an administrative necessity. Clearly, Congress could not have chosen to transfer land directly from the Bureau of Land Management to the individual Natives. Even with the Native corporations to serve as conduits, the process of land selection and conveyance under ANCSA was enormously complex and extremely slow.\(^{51}\) If Congress had permitted selection of land by thousands of individuals, the administrative task would have been essentially impossible.

Third, neither ANCSA nor its legislative history suggest any reason to consider the settlement land as inherently different from the money which the Native corporations received from the Alaska Native Fund. ANCSA expressly provides that individual Natives may receive distributions of settlement money without tax liability. Insofar as the money and the land both constitute compensation, the same logic that supports nontaxable distributions of cash from the Alaska Native Fund also supports nontaxable distributions of land or proceeds from the sale of the land. Nothing in the legislative history of ANCSA indicates that Congress wished to impose tax or other barriers to the sale of land or resources by the Native corporations. On the contrary, the legislative history suggests that “[t]he key to Native progress, and thus the single most important facet of the land settlement legislation, is money.”\(^{52}\) Congress anticipated that the corporations would sell land or interests in land, such as timber or oil, as sale is the normal means by which to realize the economic potential of such land or interests in land.\(^{53}\) If so, then the land is simply capital like any other, available for liquidation to suit the needs of the corporations and their shareholders. Insofar as a corporation may sell settlement land, there is no apparent policy reason to distinguish between money from such a sale and money from the Alaska Native Fund, for money from either source merely reflects part of the aggregate value of the settlement package.

Congress may have contemplated that some proceeds from the sale of land or natural resources would be invested by the Native corporations in assets which would provide the corporation’s shareholders with long-term support. In other words, Congress may have envisioned that Native corporations would diversify. Certainly diversifica-

\(^{51}\) See, e.g., S. REP. No. 201, 100th Cong., 1st Sess. 20, reprinted in 1987 U.S. CODE CONG. & ADMIN. NEWS 3269, 3270.
\(^{52}\) S. REP. No. 405, 92nd Cong., 1st Sess. 105 (1971).
\(^{53}\) The House Committee specifically anticipated that the Natives would choose land for its “economic potential,” which would include timber and oil. See H.R. REP. No. 523, 92nd Cong., 1st Sess., reprinted in 1971 U.S. CODE CONG. & ADMIN. NEWS 2192, 2195.
tion is ordinarily a prudent feature of corporate management. Even if this diversification occurred, there still would be no policy reason to tax distributions made possible by that diversified activity until the individual Natives had recovered the full value of the compensatory settlement transfer initially made to them.

II. THE IMMEDIATE PROBLEM: THE IRS INTERPRETATION

As the IRS interprets ANCSA, a distribution of settlement land or natural resources or proceeds from the sale of land or resources by a Native corporation is taxable in accordance with I.R.C. § 301.\textsuperscript{54} In other words, such distributions are taxable as dividend income to shareholders to the extent that the Native corporation has either current or accumulated earnings and profits. Most Native corporations have a considerable deficit in accumulated earnings and profits, largely as a result of the decline in the prices for timber and oil in the 1980's. However, a significant number of Native corporations have generated positive current earnings and profits through operation of separate businesses that the corporations have financed through the sale of land or natural resources.\textsuperscript{55} Pursuant to the current IRS interpretation of ANCSA, the shareholders of corporations with positive current earnings and profits pay income tax on a distribution of proceeds from the sale of the settlement land or natural resources. This result is inconsistent with the otherwise coherent structure of ANCSA, which establishes that compensation for the extinguishment of Native land claims is not taxable.

A. IRS Letter Rulings

In 1977, the IRS issued a private letter ruling to several Native corporations on the basic tax aspects of ANCSA.\textsuperscript{56} Although the 1978


\textsuperscript{55} The existence of current earnings and profits on the books of Native corporations is partly a matter of supposition. In other words, there are certain businesses owned by Native corporations that have become relatively well established. As Native corporations are not public, however, little hard information generally is available with respect to their finances.

\textsuperscript{56} The precise date of the ruling was February 2, 1977. The ruling has never been published. With respect to the formation of Native corporations, the IRS ruled:

1. The tax-free distribution of cash from the fund, and land by the U.S. government for the relinquishment of the aboriginal land claims of Alaska Natives and Native groups constitute payment to the qualifying Natives who will be deemed to have immediately contributed the cash and lands to the Regional and Village Corporations.

2. The deemed contributions of cash from the Fund, and land by the recipient Natives as stated in (1) above to the Regional Corporations and the Village Corporations are tax free.
amendment to ANCSA later overturned parts of the ruling that dealt with net operating losses, other aspects of the ruling remain instructive, particularly the ruling's characterization of the receipt of money and land for tax purposes.

The 1977 ruling characterized the ANCSA settlement as a transfer of money and land directly to the individual Natives, followed by an immediate contribution of all such property by the individual Natives to Native corporations in tax-free incorporations under I.R.C. § 351. In accordance with this characterization, no income tax was due from the Natives on the settlement package. This characterization also resolved the issue of each individual Native's basis in his or her Native corporation stock. The aggregate basis of stock in a Native corporation was equal to the amount of Alaska Native Fund money the corporation received plus the fair market value of land the corporation received from the Secretary of the Interior, minus the amount of any nontaxable distributions by the corporation. Each individual shareholder's basis in his or her stock, therefore, was equal to the value of his or her proportionate share of the property which the corporation received under ANCSA, subject to downward adjustment by the amount of nontaxable distributions he or she might receive from the exchanges under section 351 of the Internal Revenue Code of 1954.


57. The 1977 letter ruling precipitated the enactment of section 541 of the Revenue Act of 1978, Pub. L. No. 95-600, § 541, 92 Stat. 2763, 2887-88, which included new subsections (h) and (i) for section 21 of ANCSA. These new subsections enabled Native corporations to recognize net operating losses for taxable periods before their actual receipt of property under ANCSA. The House Conference Report explained Section 541 of the Revenue Act as follows:

Corporations formed pursuant to the Alaska Native Claims Settlement Act (ANCSA) received money from the United States and the right to select Alaskan land. The shareholders are Alaska Natives. The IRS has held that (1) the value of surveys of the land made by oil companies to assist the corporations in making their selections is income to the corporations; (2) land selection costs incurred by the corporations are not deductible but must be added to the basis for the land; and (3) other expenses of the corporations are nontaxable "start-up" costs because the corporations have not yet begun business. Because many Native shareholders are related to one another, some corporations may meet the definition of personal holding companies.

The Senate amendment provides that ANCSA corporations (1) do not include in income the value of outside surveys; (2) may deduct land selection costs; (3) are deemed to have begun business; and (4) are not personal holding companies.

The amendment is effective as of December 18, 1971. The survey income provision would remain in effect until the earlier of 1991 or the date the corporation has received all its land under ANCSA. The personal holding company provision would remain in effect until 1991.


corporation. The aggregate basis in the stock of each Native corporation equaled the corporation’s basis in the property the corporation has received pursuant to ANCSA and has not distributed.

The IRS characterization of the ANCSA settlement in the 1977 letter ruling subtly eliminates, for tax purposes, any direct entitlement to the settlement package on the part of the individual Natives. If, as the IRS supposes, the individual Natives themselves actually had received the money and land, and had contributed all such property to their corporations, they then would have exhausted their ANCSA tax exemption on their initial receipt of the property, before the property reached corporate solution. The IRS view implies that the only nontaxable compensation to the individual Natives under ANCSA was an imaginary initial transfer directly to them. Under this approach, the individual Natives have no right to receive, from the Native corporations in which they hold stock, any amount (other than distributions attributable to the Alaska Native Fund) as nontaxable compensation. In effect, the IRS takes the position that the nontaxable status of distributions of amounts from the Alaska Native Fund is mere largess rather than a manifestation of the principle that compensation for Native land claims is not taxable.

In 1981, the IRS issued a private letter ruling that dealt specifically with dividend distributions by a Native corporation. Fulfilling the implications of the 1977 ruling, the IRS ruled that a distribution traceable to the Alaska Native Fund was not taxable to shareholders but that a distribution of proceeds from the sale of timber rights which the Native corporation had received pursuant to ANCSA was taxable to shareholders to the extent of the corporation’s earnings and profits. In support of the conclusion that the distribution of proceeds from the sale of timber rights is taxable, the IRS cited section 21(d)(1) of ANCSA, which states that “[a]ll rents, royalties, profits, and other revenues or proceeds” derived from the land or interests in land a corporation has received under ANCSA are taxable in accordance with ordinary tax law.

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59. A possible alternative interpretation is that the sole purpose of the imaginary transfer of the settlement property to the Native individuals is to determine the basis of the Native individuals in their stock. Under this interpretation, the imaginary transfer would have no impact on the extent to which the Native individuals are entitled to receive nontaxable corporate distributions, up to the amount of their basis in their stock.


61. 43 U.S.C. § 1620(d)(1) (1982). As Section 1.C. of this Article points out, application of this provision to distributions of proceeds from the sale of land or interests in land is problematic.
The Native corporation that submitted the request for the 1981 ruling specified that the corporation had placed the Alaska Native Fund amounts into a special account for eventual distribution. Thus, any distributions out of this account were clearly traceable to the Alaska Native Fund. The IRS did not assert that segregation of such revenue into a special account was necessary, but the procedure is nevertheless quite consistent with the characterization of the ANCSA settlement in the 1977 ruling. In effect, the establishment of a special account treats revenue from the Alaska Native Fund as a peculiar tax-exempt asset, different from mere compensation for land claims.

In 1987, another Native corporation requested a ruling from the IRS on the tax consequences of a distribution of proceeds from the sale of timber on land which the corporation had received under ANCSA. This request specified that the corporation would incur a loss on the sale of the timber, so that the transaction would result in no taxable gain at the corporate level. Nevertheless, the IRS viewed the transaction as a distribution taxable to shareholders to the extent of the corporation’s earnings and profits. The Native corporation withdrew its request prior to issuance of a ruling.

B. Problem of Current Earnings and Profits

The problem with the IRS interpretation stems from the distinction between accumulated and current earnings and profits. Many Native corporations, especially village corporations, have lost money year after year on timber, the market price of which reached its apex about 1980, when most of the conveyances of timber land finally occurred, and then fell dramatically in the early to mid-1980's. As a result, these Native corporations carry large deficits in accumulated earnings and profits. In recent years, however, certain corporations have managed to put together profitable business enterprises quite apart from

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62. If the individual Natives have a direct entitlement to the ANCSA settlement package as compensation for extinguishment of land claims, then the dollar amount of the Alaska Native Fund should constitute nontaxable compensation both at the corporate level and at the shareholder level. As dollars are fungible, the actual source of any dollars that a corporation distributes to shareholders should not affect the tax status of the distribution. Insofar as the individual Natives have a direct entitlement to the settlement package, tracing the source of distribution dollars is unnecessary. By contrast, tracing could become necessary if assets that constitute compensation at the corporate level are generally taxable at the shareholder level. Under such a system, a corporation might have to show that the dollars of a distribution constitute special assets that are exempt from tax on distribution to shareholders. The 1988 amendments to ANCSA changed section 21(a) to provide clearly that tracing is unnecessary. See Pub. L. No. 100-241, 101 Stat. 1788, 1810 (1988).

63. The authors are aware of this ruling request as a consequence of personal involvement.
timber or other natural resources.\textsuperscript{64} Despite the existence of prior losses and an accumulated earnings and profits deficit, these business enterprises may give rise to current earnings and profits for a particular taxable year. If a Native corporation with current earnings and profits distributes land or resources or proceeds from the sale of land or resources, the distribution will result in income tax to shareholders, even though the distributee shareholders have not received, in their individual capacities, an amount equal to their proportionate shares of the settlement package.

As a general matter, I.R.C. § 301 governs taxation of shareholders on receipt of corporate distributions with respect to stock. Under I.R.C. § 301, the amount of any such distribution constituting a “dividend” under I.R.C. § 316(a)\textsuperscript{65} is ordinary income to shareholders. Under I.R.C. § 316(a), the term “dividend” includes any corporate distribution out of accumulated earnings and profits, or out of current earnings and profits. Furthermore, I.R.C. § 316(a) specifies that every corporate distribution is out of earnings and profits to the extent that the corporation has earnings and profits. Current earnings and profits reflect only revenues and expenses of the current period, without regard to historical gains or losses. It is possible, therefore, for a corporation to have positive current earnings and profits and at the same time have a deficit in accumulated earnings and profits.

Although the village corporations have compiled a dreary financial record, their distributions nonetheless may result in income tax to shareholders. The village corporations received none of the subsurface estates—no oil or mineral deposits—and virtually all of these corporations have lost money on timber. Many have exhausted their share of the Alaska Native Fund. However, these Native corporations still have a responsibility to provide income for their shareholders, most of whom remain quite poor.\textsuperscript{66} Under these circumstances, distributions

\textsuperscript{64} In many instances these new and alternative business activities were funded by proceeds from the sale of such assets.

\textsuperscript{65} I.R.C. § 316(a) (1982).

\textsuperscript{66} Unlike an ordinary corporation, a Native corporation is engrafted on a preexisting Native group. As a general matter, a Native village or other Native group is likely to function communally—or at least much more so than an ordinary corporation, which is not communal in the least. One aspect of communal operation is that an individual might look to the group as a whole for assistance. Although corporate dividends are not an ideal means through which to provide such assistance, the Natives nevertheless must attempt to reconcile the corporate form with their traditional values as best they can. Congress has acknowledged a widely held sentiment that the corporate form “frequently conflict[s] with traditional Native values and Alaska’s traditional Native cultures.” S. REP. No. 201, 100th Cong., 1st Sess. 21. \textit{reprinted in} 1987 U.S. CODE CONG. & ADMIN. NEWS 3269, 3272.
often are necessary regardless of a corporation's financial performance.

Some of the village corporations carry large deficits in accumulated earnings and profits and will not generate positive current earnings and profits in the immediate future. Distributions by such corporations will merely result in a reduction of each shareholder's basis in his or her stock. In many instances, however, village corporations have generated positive current earnings and profits through business enterprises apart from timber. Pursuant to I.R.C. § 301, distributions by any of these relatively successful village corporations will result in ordinary income to shareholders to the extent of the corporation's current earnings and profits. In light of their long history of losses, these corporations may not generate taxable income. More precisely, these corporations may have enough net operating loss carryforwards to absorb current earnings for purposes of the corporate income tax. 67

67. Under I.R.C. § 301 (1982 & Supp. IV 1986), a Native corporation that carries a deficit in accumulated earnings and profits and generates a deficit in earnings and profits for the current year may distribute land or interests in land or proceeds from their sale to its shareholders without consequent income tax liability on the part of the shareholders. As the corporation has no earnings and profits, I.R.C. § 301 treats the distribution as a return of capital, which reduces each shareholder's basis in his or her stock by the amount of the distribution he or she receives. Id. § 301(c)(2) (1982). If a distribution from the corporation were to exceed a shareholder's basis in his or her stock, the shareholder would have a taxable capital gain. Id. § 301(c)(3). In the case of Native corporations, however, a shareholder's basis generally should exceed any possible distributions of proceeds from the sale of land or interests in land because his or her basis reflects the value of these properties at the time of the initial conveyance by the Secretary of the Interior or at the time of first commercial development. See supra notes 41-42 and accompanying text. In the meantime, the value of most of these properties will have fallen with the market price of timber.

68. Until enactment of the Technical Corrections and Miscellaneous Revenue Act of 1988, Pub. L. No. 100-647, 102 Stat. 3342, certain Native corporations had been able to sell their net operating losses. Prior law, specifically section 60(b)(5) of the Tax Reform Act of 1984, allowed a Native corporation to engage in tax sharing arrangements without regard to certain generally applicable restrictions. Pub. L. No. 98-369, § 60(b)(5), 98 Stat. 494, 579, (1984), as clarified by Section 1804(e)(4) of the Tax Reform Act of 1986, Pub. L. No. 99-514, § 1804(e)(4), 100 Stat. 2085, 2801. In effect, a Native corporation was able to sell net operating losses to companies in which the Native corporation did not own significant equity. As Senator Stevens explained the purpose of the 1986 clarification in floor debate, the proceeds from the sale of net operating losses would provide an "infusion of capital [that] would allow many Native corporations to put their financial houses in order." 132 CONG. REC. S8175 (daily ed. June 23, 1986). By 1988, the tax sharing arrangements had become controversial, mostly because the revenue cost had been much higher than the initial estimate. So You Thought Big Tax Loopholes Disappeared in '86?, Wall St. J., Aug. 19, 1988, at 1, col. 4. In the 1988 Act, Congress repealed the provisions that allowed such tax sharing arrangements, except with respect to certain contracts entered before July 26, 1988. The repeal of these provisions is not strictly relevant to the subject matter of this Article. However, the tax sharing arrangements themselves may have produced income for certain corporations as well as earnings and profits, and thus may have accelerated the need to address the tax consequences of distributions that reflect the value of land and interests in land.
As net operating loss carryforwards do not affect current earnings and profits, these corporations can generate positive current earnings and profits despite the existence of a net loss for income tax purposes.

C. Need for Legislative Clarification

Insofar as application of I.R.C. § 301 imposes income tax on amounts that reflect the value of ANCSA land or resources, or proceeds from the sale of such land or resources, the IRS view is inconsistent with the central principle that compensation for Native land claims is not taxable. The land and resources constitute compensation, whether retained in corporate solution or passed on to shareholders. Therefore, taxation on the value of the land and resources is simply inappropriate. Application of the general corporate tax law of earnings and profits to distributions by Native corporations is unfair because the Native shareholders did not become shareholders voluntarily. Ordinarily, taxpayers choose whether to invest in corporate or noncorporate enterprises and whether or not to invest in particular corporations. If a corporation experiences losses, shareholders may realize those losses (at least as capital losses) by selling their shares. Unlike ordinary taxpayers, however, Alaska Natives did not choose to invest their individual portions of the ANCSA settlement in shares of Native corporation stock. The corporate structure was thrust upon them. Moreover, individual Natives generally are not free to liquidate their Native corporation stock.

The establishment of the Native corporations did not alter the compensatory character of the assets with which the government capitalized these corporations. Congress designed ANCSA's corporate system merely as a workable administrative vehicle for the settlement of land claims. Surely Congress did not consciously intend that the administrative vehicle would operate indirectly to take away, in the form of taxes, part of the value of the compensation offered to the Natives.

Finally, the imposition of income tax on distributions by a Native corporation that reflect the value of land which the corporation has received under ANCSA is inappropriate because such taxation discourages prudent corporate management. A Native corporation can avoid having current earnings and profits by disposing of its rights to land and natural resources at a loss and then distributing the proceeds. Today, a Native corporation ordinarily would incur a loss on a sale of land or natural resources for tax purposes because the value of these assets has declined greatly since the conveyance of the assets to the
corporations, the event that establishes each corporation's basis. Shareholders would not receive a dividend for tax purposes through distribution of proceeds from such a sale because the distributing Native corporation would have had no earnings and profits. There would be no capital gain to shareholders because each shareholder would have a basis in his or her stock equal to his or her aliquot share of the corporation’s basis in its land and natural resources, so that the distribution to each shareholder would not exceed the shareholder’s basis in his or her stock.

If Native corporations do liquidate, they will eliminate tax for their shareholders, who will enjoy a one-time-only burst of prosperity, followed, in many cases, by destitution. Surely this cannot be what Congress intended in 1971, or intends currently. If Alaska Natives, who had their old way of life taken from them under ANCSA, are to have any meaningful chance of making the transition to other ways of life while maintaining personal and economic dignity, the Native corporations must provide support and assistance for some time to come. Yet the shareholders of the prudent corporations who defer short-term prosperity in exchange for a meaningful long-term chance of survival with dignity are, in effect, penalized under the IRS approach. They would be forced to pay taxes on the interim support which they receive from their Native corporations, even though each Native's economic position is actually worse (because of losses realized at the corporate level) than at the time of the 1971 settlement. Such a result would not occur if ANCSA's tax provisions were to recognize that individual Natives, as opposed to Native corporations, are entitled to both money and land in settlement of aboriginal land claims.

III. THE LEGISLATIVE SOLUTION: TWO PROPOSALS

To clarify current law, Congress should amend ANCSA to permit Native corporations to distribute their ANCSA land or resources, or proceeds from the sale of land or resources, without income tax liability to shareholders to the extent of the Native corporation’s basis in such land or resources. Each of the two proposals herein, the “Full Compensation” proposal and the “Proceeds of Sale” proposal, would provide for nontaxable distributions. Moreover, the amount a shareholder receives in nontaxable distributions under each proposal would reduce the shareholder's basis in his or her stock. The difference between the two proposals lies in their respective formulas for determination of the cap on nontaxable distributions.
A. Full Compensation Proposal

The simplest approach is to amend section 21(c) of ANCSA to provide that distributions by a Native corporation, up to an amount equal to the corporation's basis in the land or interests in land which the corporation has received pursuant to ANCSA, are not subject to any form of taxation. Under this approach, the land portion of the settlement package would become as accessible to shareholders of Native corporations as revenue from the Alaska Native Fund. The full value of the nontaxable compensation a Native corporation has received on behalf of its shareholders could reach these shareholders as nontaxable compensation, without regard to the corporation's earnings and profits. In essence, Native shareholders would be permitted to recover their basis in their shares of Native corporation stock without tax. Any nontaxable distributions would reduce the amount of their basis and therefore would reduce the amount of nontaxable dividends which Native shareholders could receive in the future.

The Full Compensation proposal recognizes a direct entitlement on the part of individual Natives to a share of the entire settlement package. This proposal does not require a Native corporation to trace distributions to particular property that the corporation has received pursuant to ANCSA. In effect, a Native corporation could distribute cash that reflects the value of land or interests in land which the corporation has received pursuant to ANCSA prior to any disposition of such land or interests by the Native corporation. The only limitation on nontaxable distributions under this approach is the dollar cap equal to the Native corporation's total basis in such land or interests. The Full Compensation approach treats money and land as interchangeable, and focuses only on the amount of the compensation Congress intended the Native individuals to receive.

Example: A Native corporation has received land worth $300X at the time of receipt, which consisted of $20X in land value and $280X in timber value. At the same time, the Native corporation received $40X from the Alaska Native Fund. As the value of the land was not higher at the time of first commercial development of any timber resources, there was no occasion for a step-up in basis. Therefore, the corporation's basis in all of its settlement property is $340X. Under the Full Compensation proposal, the Native corporation could distribute up to $340X from any source and the shareholders would receive such distributions as nontaxable compensation, not as taxable dividends. Distributions to shareholders in excess of $340X would be taxable to shareholders in accordance with generally applicable tax
If the corporation had distributed $50X that was nontaxable (due to the absence of earnings and profits) in prior years, the corporation could distribute up to $290X from any source as nontaxable compensation in the future.

**B. Proceeds of Sale Proposal**

An alternative approach is to amend section 21(c) of ANCSA to provide for nontaxable distributions commensurate with the Native corporation’s proceeds from the sale of land or interests in land that the corporation has received pursuant to ANCSA. Under this approach, a Native corporation’s distribution of proceeds from the sale of such land or interests in land would not result in taxation at the shareholder level except insofar as the distribution exceeded the corporation’s basis in such land or interests. In practical terms, each Native corporation would maintain an account on its books for all proceeds from the sale of such land or interests in land. The dollar amount of this account at any particular time would reflect the amount available for nontaxable distributions to shareholders, except to the extent that this amount might exceed the corporation’s basis in the property the corporation has sold.

If a corporation’s land and resources decline in value, the corporation will obtain less in sale proceeds and the amount of the proceeds account may fall below the corporation’s basis in the land and resources the corporation has sold. As a result, the amount of nontaxable distributions under the Proceeds of Sale proposal is potentially less than the full amount of a Native corporation’s basis in ANCSA property. Within a Native corporation’s proceeds account, profit on one sale of land or resources potentially could offset loss on another. Thus, a corporation might incur a loss on its first sale, so that the proceeds account would fall below the basis of the property the corporation has sold, but a gain on the second sale could raise the proceeds account so as to equal or exceed the total basis of property the corporation has sold. After the second sale, the corporation could distribute the full amount of its basis as nontaxable compensation.

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69. Prior to any nontaxable distributions, the aggregate basis in the corporation’s stock is $340X. Each shareholder must reduce his or her basis in his or her stock by the amount of any nontaxable distribution to him or her. If the corporation distributes the full nontaxable $340X to shareholders, in equal amounts per share, then each shareholder should have a zero basis in his or her stock.

70. The Proceeds of Sale proposal does not contemplate that a corporation must establish a separate bank account but only a special account in the corporation’s own books. Under this proposal, a corporation could distribute amounts from general corporate funds.

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Example: A Native corporation has received land worth $300X at the time of receipt, which consisted of $20X in land value and $280X in timber value. At the same time, the Native corporation received $40X from the Alaska Native Fund. The Native corporation has previously distributed $50X, which was not treated as a taxable dividend because the corporation had no earnings and profits. To date, the Native corporation has sold three-quarters of the timber, realizing $150X after expenses. Basis attributable to this timber is $210X. Pursuant to the Proceeds of Sale approach, the aggregate amount of proceeds that could be distributed as nontaxable compensation is $190X ($40X from Alaska Native Fund and $150X from the sale of timber) minus $50X (the amount previously distributed), or $140X. If the corporation were to sell any remaining timber or other property, the net proceeds from such sales would serve to increase that amount the corporation could distribute as nontaxable compensation, although this amount could never exceed $340X (the original basis of the settlement property received plus the $40X from the Alaska Native Fund).

C. Comparison of the Two Proposals

Both the Full Compensation proposal and the Proceeds of Sale proposal seek to resolve the ambiguity under ANCSA regarding the taxation to the individual Natives of the amounts which were transferred to the Natives in extinguishment of their aboriginal land claims. The Full Compensation proposal recognizes a direct entitlement to the settlement package and permits the individual Natives to receive nontaxable distributions up to the original value of the settlement package, without regard to the performance of the Native corporations or the value of corporate assets. The Proceeds of Sale proposal treats ANCSA land and resources as nontaxable assets, but further provides that the amount which may be distributed as nontaxable compensation is subject to erosion by market forces. Where the value of timber and oil has fallen, the Proceeds of Sale proposal would allow less in the way of nontaxable distributions. Under this approach, the Native shareholders would bear the brunt of the decline in value which is realized as the assets are converted to cash.

Both proposals contemplate a limitation on the amount which any Native corporation may distribute as a nontaxable distribution. Both proposals contemplate that the maximum amount so distributable is equal to the corporation’s basis in such land or interests. Under the Full Compensation approach, this maximum is completely static. The shareholders retain the capacity to receive the maximum in nontaxable
distributions over the life of the corporation, regardless of what happens at the corporate level. The Full Compensation approach is thus consistent with section 21(a), as amended, which now allows a corporation to distribute its revenue from the Alaska Native Fund without segregation of such revenue into a special account.

Under the Proceeds of Sale approach, the cap on nontaxable distributions floats depending on the net value which is realized from the sale of the land or interests in land transferred to the Native corporations as compensation. The Proceeds of Sale approach results in the creation of a running account which will measure the net value which the Native corporation has realized from the sale of the property transferred to it. Any prior nontaxable distributions are treated as distributions from such net proceeds. Thus, prior nontaxable distributions reduce the amount that can be distributed as nontaxable compensation in the future.

While both proposals are reasonable, the Full Compensation proposal is superior for two reasons. First, the Full Compensation proposal is more equitable because market forces would not directly affect an individual Native's entitlement to nontaxable compensation. This proposal assures that if and when the individual Natives actually receive their full measure of compensation through distributions from the Native corporation in which they hold stock, they will not incur income tax as a result. The Natives did not choose corporate form. The amount of compensatory distributions to them should not depend on the eventual market price of timber or oil. Second, the Full Compensation proposal is somewhat less complex because the amount that could be distributed as a nontaxable distribution would remain static.

IV. CONCLUSION

Congress should amend ANCSA to provide expressly that a distribution by an Alaska Native corporation is not taxable income to individual Native shareholders insofar as the distribution reflects the value of land or interests in land which the corporation has received pursuant to ANCSA. The best approach is simply to specify by amendment that distributions by an Alaska Native corporation, up to an amount equal to the corporation's basis in its ANCSA land or resources, are not subject to any form of taxation. Such an amendment would complete an otherwise comprehensive ANCSA policy against the imposition of income tax on compensation for the extinguishment of aboriginal land claims and would help assure that the individual
Natives actually receive the full measure of compensation that Congress originally intended to convey.