TIPS FOR NATIVE AMERICAN ENTREPRENEURS

Business Formation

Whether starting a new business or managing growth in an existing one, choosing the correct business structure can help your enterprise prosper. There are **four basic business structures**: sole proprietorship, general partnership, limited liability company (LLC), and corporation (Inc.). Important issues to consider include taxes, liability, and financing. In addition, the overlay of tribal law and regulation adds a layer of complexity.

Sole Proprietorship

A sole proprietorship always has one owner and is the most common business structure. No action is required to form a sole proprietorship. Merely doing business is enough to establish this business type. In legal terms, there is no difference between the company and the owner.

Taxes: The business owner pays taxes on the business as part of her ordinary income tax.

Liabilities: Since there is no legal difference between the business and the owner, the owner is personally liable for all debts, judgments, and obligations. This means the owner's personal belongings can be lost or forfeited to cover business debts.

Financing: Obtaining financing for a sole proprietorship can be challenging. Typically, sole proprietorships are new companies or small businesses without a long history of successful business operations which a bank may evaluate. Also, banks are reluctant to loan money to a sole proprietorship because they often lack the collateral necessary to secure the loan.

TRIBAL GOVERNANCE OVERLAY

Taxes: Tribal members are **generally exempt from state income taxes.** However, business conducted off tribal lands likely will be subject to state taxation. This is important to remember because you may be subjecting your income to state taxation. Tribal members are, however, **subject to federal income taxes and tribal taxes.** A sole proprietorship's taxing structure means that any money made will be viewed as individual income and thus subject to the appropriate federal and tribal taxes.

Financing: Physical or real property (e.g., land and houses) is often used to start or grow a business. Due to landownership's nature on tribal lands, tribal members may find it difficult to obtain traditional loans or financing necessary to start or grow their company.

Pros: 1) Inexpensive and straightforward to start; 2) Simple taxation; 3) Tribal members may not be subject to state taxation.

Cons: 1) Business owner is personally liable for debts and settlements; 2) May be difficult to obtain financing, especially on tribal lands.

PLEASE NOTE: This handout does not offer or substitute for legal advice. For more information: CALS-RuralStudies@uidaho.edu.

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General Partnership

A general partnership has more than one owner and is the most common business structure for partnerships. They are very similar to sole proprietorships in taxation and liabilities but differ slightly in that a general partnership can own property that is separate from the partners' property. Partners are not required to file any paperwork to be legally recognized. However, partnership agreements are relatively simple and advisable, so that all partners are clear on what is required of them and what they can expect in return.

In the absence of any formal partnership agreement, states and some tribes have laws that act as default rules for items such as ownership, profit sharing, and distributions. Typically, in the absence of a partnership agreement, ownership and profit sharing will be fifty-fifty despite initial investment levels.

Taxes: The business owner pays taxes on the business as part of her ordinary income tax.

Liabilities: General partnership owners are personally liable for all debt, judgments, and obligations of the partnership. However, property owned by the partnership is typically the first to be foreclosed. If there is a balance remaining after all business property has been taken, the owners' private assets may be in jeopardy. In addition, partners are "jointly and severally" liable. This means partners are individually liable for the business's entire debt; if one partner cannot pay their share of the debt, other partners are held responsible.

Financing: General partnerships face many of the same problems that sole proprietorships face when trying to obtain financing. They are often new companies with few assets to use as collateral. However, the ability to pool resources may reduce these barriers.

TRIBAL GOVERNANCE OVERLAY

Taxes: Tribal members are **generally exempt from state income taxes.** However, business conducted off tribal lands likely will be subject to state taxation. This is important to remember because you may be subjecting your income to state taxation. Tribal members are, however, **subject to federal income taxes and tribal taxes.** A general partnership's taxing structure means that any money made will be viewed as individual income and subject to the appropriate federal and tribal taxes. A tribal member's tax liabilities are not affected if another partner is not a tribal company member, since general partnership income is viewed as individual income.

Financing: Physical or real property (e.g., land and houses) is often used to start or grow a business. Due to landownership's nature on tribal lands, tribal members may find it difficult to obtain traditional loans or financing necessary to start or grow their company.

Pros: 1) Inexpensive and straightforward to start; 2) Simple taxation; 3) Tribal members may not be subject to state taxation.

Cons: 1) Business owners are personally liable for debts and settlements; 2) May be difficult to obtain financing, especially on tribal lands; 3) Partners are jointly and severally liable.

Limited Liability (LLC)

Businesses usually form a Limited Liability Company (LLC) to limit members' personal liability. The LLC is distinct from its members, so its debts, obligations, or other liabilities are solely the LLC's responsibility. With a few exceptions, members or managers are not directly or indirectly liable. An LLC is a pass-through entity, meaning it receives all income and distributes it to LLC members for tax purposes. The duration of an LLC can be for a set period or perpetual. Usually, an LLC is treated as a pass-through entity for federal income tax purposes. This means the tax attributes are passed down from the entity to its owners in proportion to their ownership interest. However, an LLC could elect to be treated as a corporation if you submit IRS Form 8832. Thus, depending on the elections made by the LLC and the number of members, the IRS will treat an LLC as either a corporation, partnership, or sole proprietorship. To learn more about LLC, please read University of Idaho Extension Bulletin 1011 (https://www.extension.uidaho.edu/publishing/pdf/BUL/BUL1011.pdf).

Corporation (Inc.)

A corporation is considered a "legal person" and is designed to offer liability protection for its shareholders. Corporations can be publicly traded or privately owned; they can be owned by thousands of shareholders or closely held (i.e., they are owned by very few people or even one person). All fifty states have laws that govern corporate entity rights and require corporations to register with the state. Corporations have articles of incorporation that govern almost every aspect of how each operates.

Taxes: Since a corporation is considered a legal person, the corporation must pay state, federal, and tribal taxes, if owed. In addition, shareholders must pay taxes on dividends, distributions, or salaries drawn from the corporation. This is known as *double taxation* and is a crucial difference between LLCs and corporations.

Liabilities: Corporations are intended to shield shareholders from the debts and liabilities of the corporation. As a legal person, the corporation is fully liable for all debts and obligations.

Financing: The act of shielding shareholders from the corporation's liabilities promotes the corporation's ability to raise capital. When a shareholder invests in a corporation, the only money she risks losing is the money used to buy the shares. This feature promotes investment in corporations and many corporations finance themselves by selling shares.

TRIBAL GOVERNANCE OVERLAY

While the Nez Perce and Coeur d'Alene tribes offer provisions in their tribal codes for nonprofit corporations, they do not provide provisions for other kinds of corporations. This means a corporation needs to be formed under state laws outside the jurisdiction of the tribe and will be subject to state taxation even if business is conducted solely on tribal lands. Additionally, a corporation wishing to do business on tribal lands will need approval from the tribe and possibly the Bureau of Indian Affairs.

Pros: 1) Limited liability; 2) May offer a way to capitalize the business.

Cons: 1) Subject to double taxation; 2) Complicated to start; 3) Complicated reporting requirements; 4) Tribal members may be subject to state taxation; 5) Local tribal codes only cover nonprofits.

A Caveat

The outcome of *Big Sandy Rancheria Enterprises v. Becerra,* a case currently before the Ninth Circuit Court of Appeals, could have significant implications for a state's authority to tax tribes and may render some of the information in this handout invalid.

Sources

Karen J. Atkinson and Kathleen M. Niles. *Tribal Business Structure Handbook* (2008); Chapter 36 in William J. Rich and Chester James Antieau, eds. *Modern Constitutional Law,* 3rd ed. (updated December 2020). St. Paul, MN: Lawyers Cooperative.

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