California Taxation of Tribal Gaming Income and Residency: Lessons from the OTA Decisions in Appeal of R. Garcia and M. Garcia

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Generally, an enrolled member of a federally recognized Indian tribe who resides on his or her tribe's reservation in California is subject to California personal income tax, except with respect to income derived from sources within the tribe's reservation. See *McClanahan v. Arizona State Tax Commission*, 411 U.S. 164 (1974).

In Legal Notice 2015-1, the California Franchise Tax Board set out its position on whether an enrolled member of a federally recognized Indian Tribe is living on or off the reservation for California personal income tax purposes. The FTB articulated four scenarios and stated that the FTB would apply the "closest connections" test articulated in *Appeal of Stephen Bragg*, 2003-SBE-003 and other Board of Equalization cases to determine whether a tribal member would be treated as residing on a tribal reservation.

The Garcia Opinions

In *Appeal of R. Garcia and M. Garcia*, 2026-OTA-0021P and 2026-OTA-0022P, the California Office of Tax Appeals ("OTA") issued two precedential opinions addressing whether an enrolled tribal member is taxable on his share of the tribe's gaming income.

The first precedential opinion addressed whether Mr. Garcia was taxable on his share of tribal gaming income. The second opinion addressed the Garcias' broader contention that the FTB lacked authority to tax tribal gaming income regardless of residency. While the taxpayers focused on the asserted immunity of tribal gaming income, the FTB centered its case on whether Mr. Garcia's closest connections were on or off the reservation.

Facts

Mr. Garcia is an enrolled member of the San Manuel Band of Mission Indians, located in San Bernardino, California. The tribe owns the Yaamava' Resort & Casino in Highland, California. As a tribal member, Mr. Garcia receives a per capita share of profits from tribal gaming operations.[1]

For years 2010, 2011 and 2012, Mr. and Mrs. Garcia filed joint California resident income tax returns. The returns excluded Mr. Garcia's income from tribal gaming revenues. The FTB proposed assessments of $223,772 for 2010, $191,070 for 2011, and $198,292 for 2012, asserting that as California residents, Mr. Garcia was taxable on all income from whatever

[1] Since 2003, the San Manuel Band has contributed over $300 million to neighboring communities in San Bernardino and Riverside Counties and other Indian tribes for education, health, economic development and cultural projects. See, https://calchamberalert.com/2023/06/30/san-manuel-band-of-mission-indians/.

source derived, including his share of tribal gaming revenues, under Rev. & Tax. Code §17041.

The Garcias Appealed to the OTA.

Besides testifying during the evidentiary hearing, Mr. Garcia submitted several declarations concerning his residency during the years in issue.

During the years at issue, Mr. Garcia attended university in New York City. The Garcias spent the academic year and much of the summer in New York, returning to California for several weeks during the summer. Mr. Garcia asserted that the reservation was his principal residence.

The Garcias owned multiple residences including:

1. A home on the reservation
2. A 4,600 square foot home in San Juan Capistrano (where they would go to on weekends).
3. A 2,374 square foot home in Huntington Beach, California,
4. An 1,829 square foot home in Newport Beach, California,
5. A property in Mission Viejo, and
6. A residential condominium in New York City.

He and his wife also visited family in Orange County.

Mr. Garcia was actively involved in two clothing design businesses in New York City and was a non-active partner in a music business in Los Angeles.

The Garcias filed federal and California resident returns listing a post office box in Patton, California, near the reservation, as their address. Their returns were prepared by a local return preparer in Patton. Mr. Garcia's driver's license listed the San Juan Capistrano home address.

Mr. Garcia did not maintain any records showing the number of days spent on versus off the reservation while in California. The FTB analyzed credit card and bank transactions in California and concluded that approximately 92% of the days with transactions were near San Jaun Capistrano and 2% occurred near the reservation. Mr. Garcia testified that this disparity was due to limited commercial activity on the reservation.

Discussion-The Jurisdictional Arguments

The taxpayers advanced four arguments as to why the FTB could not tax tribal gaming income of a registered tribal member.

1. Indian Commerce Clause. The OTA held that, under Art. III, Sec. 3.5 of the California Constitution, administrative agencies lack authority to declare a California statute or regulation unconstitutional. Accordingly, the OTA, as an administrative agency, had no jurisdiction to determine whether Rev. & Tax Code §17041 was unconstitutional.

2. Federal Preemption under IGRA. The OTA similarly held that it lacked jurisdiction to determine whether the Indian Gaming Regulatory Act ("IGRA") preempted §17041.

3. Apportionment under *Colville*. The taxpayers argued that *Washington v Confederated Tribes of the Colville Indian Reservation*, 447 U.S. 134 (1980), required apportionment of gaming income between on-reservation and off-reservation activity. The OTA rejected this argument, holding that *Colville* does not authorize apportionment of per-capita gaming income based on time spent on and off the reservation and reiterating its constitutional limitations.

4. Underground Regulation. Finally, the taxpayers argued that the FTB's approach constituted an "underground regulation." The OTA concluded that it lacked jurisdiction to require apportionment or to invalidate the FTB methodology on that basis.

Discussion: The "Residency" Case

The OTA reaffirmed that California may tax tribal-source income of a tribal member who resides off the tribal reservation. The taxpayer bears the burden of proving residence on the reservation for "all or a portion of the years at issue."

The OTA recognized that there were no California cases or statutes "that specifically define where a taxpayer 'resides' for the purpose of determining whether the taxpayer resides on their tribe's reservation." Absent a controlling statute or court decision, the OTA looked to whether Mr. Garcia's closest connections were with the reservation as opposed to San Juan Capistrano using the factors set forth in *Appeal of Stephen Bragg*, 2003-SBE-003.

The OTA found:

- No reliable evidence of time spent on the reservation.
- No travel records, third party testimony or corroborating documentation.

- No evidence showing whether Mr. Garcia returned to the reservation or to other California properties during breaks from New York.
- No evidence showing the reservation home was his principal California residence.

The OTA noted that the parties treated the taxpayer's time in New York as a temporary or transitory absence from his home in California and that he was a California resident during the years in issue.

The OTA rejected Mr. Garcia's uncorroborated testimony as insufficient and held that the taxpayers failed to show that Mr. Garcia was physically present on the reservation for any significant periods of time during the years in issue. Although some factors were mixed or neutral, the evidence showed that Mr. Garcia spent the majority of his time off the reservation, with business, property and daily life centered elsewhere. While Mr. Garcia's business interests were in New York City and California, he had significant ties to the reservation. Thus, this factor was deemed neutral. Moreover, financial transactions on and off the reservation provided little guidance since there were few opportunities to spend money on the reservation.

Accordingly, the OTA held the taxpayers failed to rebut the FTB's determination that Mr. Garcia's closest connections were off reservation. The proposed deficiencies were, therefore, sustained.

Conclusion

The central question—whether California ultimately has authority to tax a tribal member's per-capita share of tribal gaming income—will be resolved by the California courts, not administrative agencies. The key take-away, however, is clear. It is incumbent on a taxpayer who claims to be a nonresident of California to keep good records of the time spent in and outside the state and, for the periods in California, the reason for being in California. Taxpayers asserting non-residency or reservation residency must maintain contemporaneous records of physical presence, corroborating testimony, and objective evidence demonstrative where they actually lived.

As the FTB continues to intensify its scrutiny of taxpayers claiming non-residency, taxpayers must recognize that intent alone is not enough. Residency determinations are fact-driven and often decided on the strength, consistency, and credibility of the taxpayer's actions. Early planning, disciplined execution, and careful documentation can make the difference between a successful change of residency and a costly, protracted dispute. California taxpayers currently facing an FTB residency audit should seek advice from experienced counsel to avoid missteps that can undermine otherwise defensible residency positions.

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