



ITG News

Keeping First Nations Informed



Publication 4267D
Catalog Number 37831N Great Plains Edition October 2005

Message From The Director



IN THIS ISSUE

October marks the start of FY 2006 for the federal government, and with it, another annual Work Plan for the office of Indian Tribal Governments. As in past years, our Work Plan outlines the areas where we will place an emphasis for the upcoming 12 month period, and is based on an analysis of customer input, employee input, and data.

Several areas of focus will continue from this past year. This includes issues such as tip reporting by employees of tribal enterprises, and employment tax examinations. In addition to these issues, we will be placing an increased emphasis on two other significant areas:

- Bank Secrecy Act - the federal government continues to focus on combating money laundering. Due to the potential use of tribal enterprises (particularly tribal casinos) as vehicles for money laundering, we will seek to work closely with tribes to ensure that they have effective BSA Compliance Plans.
- Information Reporting - as tribal economies continue to grow, we will focus resources on ensuring that tribes are in compliance with both information reporting and withholding requirements on payments to vendors and individuals.

FY 2006 will also mark the rollout of an initiative to allow tribal entities to perform their own Compliance Checks. Detailed information on that program is available on page 2 of this newsletter.

As always, a copy of the ITG Annual Work Plan will be posted on our web site at www.irs.gov/tribes, and I welcome any questions or feedback you may have on our operations, by contacting me at (202) 283-9800, or via e-mail at christie.jacobs@irs.gov.

Message from the Director	1
Self Compliance Check Program	2
Customer Satisfaction Survey Update	3
Mitigating Financial Risk with Vendor Contracts	3
Tribal Council Payments-Treatment & Reporting	4
Land Leases in Indian Country	5
Student FICA Exception	6
Tax Calendar for the 4th Quarter	7/8

Christie Jacobs



ITG to Implement Self-Compliance Check Program

One of the cornerstones of our interactions with tribal entities has been “Compliance Checks”. While participation in Compliance Checks is voluntary on the part of tribal entities, many of them have found it to be a useful tool in determining potential weaknesses in their federal tax administration responsibilities. These have often led to additional activities such as educational seminars by ITG for tribal staff, assistance by ITG in filing returns, and adjustments to tax accounts. During the past 3 years, ITG has performed over 700 Compliance Checks, which in turn have led to nearly 800 actions to assist tribes in improving tax compliance.

We are pleased to announce that we will be implementing an initiative to permit certain tribal entities to perform their own Compliance Checks if they so choose. Tribal entities must be current in the filing of all required federal tax returns, and must have fully paid all federal tax liabilities in order to qualify. They will be able to apply to perform a “self-Compliance Check”, by submitting a request through a special link on the landing page of the ITG web site, or by notifying ITG in response to a contact we might initiate.

A special template with fill-in-the blank responses has been created, and is currently being tested by three tribes that volunteered to assist with this process. We also are creating a special web page with linkages to reference material that will assist tribes in both understanding the process, as well as in completing their own Compliance Check.

As part of this process, tribal entities performing their own Compliance Check will have the opportunity to effect any corrective actions. An ITG Specialist will assist in that process, and will mitigate any penalties wherever possible. For example, if a tribal entity discovered during a self-Compliance Check that they had not filed required Forms 1099, the entity could make a self correction without risk of penalty.

We worked with several tribes during the development of this initiative, and we believe that there are several advantages that a tribe might realize through this process. Among them are:

- Existing tribal finance staff might gain added insights into key federal tax administration issues that impact their positions and the tribal entity.
- A new tribal finance officer could utilize a self-Compliance Check to establish a baseline of current federal tax compliance. It would improve their knowledge of the tax issues within the specific entity, and allow them to remedy any problems that might pre-date their assumption of tax responsibilities.
- A tribal entity might identify a potential area of noncompliance that they wish to surface to ITG and remedy with minimal risk or cost.

We will be posting information to our main landing page at www.irs.gov/tribes as soon as this initiative is ready to launch nationwide, and a Special Edition of ITG News will be issued as well. We plan to be ready by mid-November, and sincerely hope that this initiative will empower tribes to self-assess federal tax compliance and effect improvements. We thank those who have been involved in its design and testing, and look forward to active participation of tribal entities who believe they might benefit.

Consultation Policy Update

We continue to progress with the issuance of an IRS/Tribal Consultation Policy. While we continue to work through the clearance process internally and with the Treasury Department, we plan to begin to implement the section of the policy that will direct a minimum of four annual listening meetings. Our web site will contain the latest news as we move forward to finalize the policy, as well as schedule the initial meetings.



Annual Customer Satisfaction Survey Update

As we announced in the July issue of ITG News, we undertook our annual customer satisfaction survey of all 564 federally-recognized tribes during August and September, in order to secure feedback on our operations. As noted in the “Message From The Director” in this issue, feedback from tribes is one component we use in formulating our annual Work Plan.

We are just beginning to analyze the responses, and as in past years, we will publish the results on our web site at www.irs.gov/tribes. Our report, which we plan to complete and post by November 15th, will contain a summary of any actions we will undertake to effect improvements based on the feedback provided by tribes. Improvements made as a result of past surveys include staffing increases, creation of new educational products, and the redesign of the ITG web site. Equally important is survey feedback on areas where we are meeting the federal tax administration needs of tribes, so that we can continue to reinforce our activities in those areas.

We want to thank all of you who took the time to respond. While we welcome your feedback at any time, your survey input is valuable in our decision-making processes. We look forward to your continuing participation in this important process.

Effective Internal Controls Can Mitigate Risk in the Contracting Process

Several tribes have surfaced concerns with losses they incurred from contractors who failed to perform services as required. Subsequent discussions revealed that in many cases the tribes did not have adequate controls in place to properly award or monitor the contracts. While tribes enact their own operating procedures for contracting with vendors, many have developed internal controls that help ensure the contracting process has four key steps – solicitation of bids for statements of work, a formal award of the contract by a duly designated tribal body, a validation of work performed, and a documented formal payment process. Generally the award and monitoring of performance is done by a different party than the one that makes payment. A certification is used to validate that the work is completed and to request issuance of payment.

While there is no guarantee that losses can be avoided, the creation of internal checks and balances within the process by the tribe can help ensure that work is performed as required, and that payment is not made until the tribe is satisfied that the contract has been fully performed.

Reporting Abuses/Schemes

We continue to work with tribes and tribal officials to address financial abuses and schemes being promoted in Indian country. Working together can help ensure the integrity of tribal finances, and eliminate the threats posed by individuals with schemes that appear “too good to be true” and often are. If you are aware of financial impropriety, or of a promoter advocating a scheme that appears highly suspect, you can contact the ITG Abuse Detection and Prevention Team at (716) 686-4860, or via e-mail at tege.itg.schemes@irs.gov

Publication 4268—Employment Tax Guide for Tribes

Our on-line Employment Tax Guide continues to receive a very positive response from tribal payroll and finance employees. You can download this comprehensive guide from a link on our landing page at www.irs.gov/tribes.



Treatment and Information Reporting of Tribal Council Member Payments Made by Indian Tribal Governments

Revenue Ruling 59-354 explains that monies paid for services performed as tribal council members (e.g. monies paid to attend council meetings) **do not constitute wages** for purposes of **FICA** or **income tax withholding**. Such payments, however, are considered income and are **subject to federal income tax** regardless of whether tax was withheld or a Form W-2 was issued. These monies are reported as income on Form 1040, Line 7. Use **Form W-2** to report income from meeting stipends if the combined amount of the meeting stipends plus Tribal government wages is **\$600 or more** in a calendar year. Please refer to Treasury Regulation 1.6041-2(a)(1) to review the \$600 W-2 reporting rule in further detail. **Do not** report meeting stipends on Form 1099-Miscellaneous. Please note that tribal council members may **voluntarily elect** to have income tax withheld from their meeting stipend payments.

Hopefully, the following examples will help clarify any questions you may have.

Situation 1: A Tribal government pays an individual \$200 in a calendar year for meeting stipends as a tribal council member. The Tribal government does not employ the council member in any other capacity.

Neither FICA tax nor income tax withholding applies to the \$200 payment. Because the council member earns fees that are less than \$600, the Tribal government is not required to issue Form W-2, but the individual must still report the income on their federal income tax return.

Situation 2: A Tribal government pays a tribal council member \$1,100 in the calendar year for meeting stipends. The Tribal government does not employ the council member in any other capacity.

Neither FICA tax nor income tax withholding applies to the \$1,100 paid to the council member for the calendar year. Box 1 of Form W-2 will reflect \$1,100 for meeting stipends. There are no entries in boxes 2, 3, 4, 5, or 6 (or you can enter zeros if you prefer). Enter "Revenue Ruling 59-354" in Box 14 of Form W-2. The employee must report the full \$1,100 as wages on their federal income tax return.

Situation 3: A Tribal government pays a council member \$200 in a calendar year for meeting stipends. The Tribe also employs the council member in another capacity in which the employee earns wages of \$300 that are subject to FICA tax and income tax withholding.

Neither FICA tax nor income tax withholding applies to the \$200 paid to the employee for services as a tribal council member, but the \$300 payment for wages is subject to FICA tax and income tax withholding. The Tribal Government must report on Form W-2 the \$300 payment for wages and the amounts of tax withheld. The \$200 payment is not required to be reported on Form W-2 because the total of the two payments is less than \$600 for the calendar year. However, the full \$500 must be still reported by the employee on their federal income tax return.

Situation 4: A Tribal government pays a council member \$200 in a calendar year for meeting stipends. The Tribe also employs the council member in another capacity in which the employee earns wages of \$500 that are subject to FICA tax and income tax withholding.

Neither FICA tax nor income tax withholding applies to the \$200 paid to the employee for services as a tribal council member. The \$500 payment for wages is subject to FICA tax and income tax withholding. Because the total of the two payments is \$600 or more for the calendar year, the Tribal government must report on Form W-2 both the \$200 and the \$500 payments, and the amounts of tax withheld. Box 1 of Form W-2 will reflect \$700 for total wages, Box 3 will reflect \$500 for FICA wages, and Box 5 will reflect \$500 for Medicare wages. The applicable federal income tax withheld will be shown in Box 2, while Boxes 4 and 6 will reflect the FICA and Medicare tax withheld. Enter "Revenue Ruling 59-354" in Box 14 of Form W-2. The full \$700 must be reported by the employee on their federal income tax return.

The Tribal government may choose to file more than one Form W-2 for Situation 4 in order to report the income from meeting stipends and Tribal government wages separately.



Land Leases in Indian Country

Federally recognized Indian tribes are governments and thus not subject to federal income tax. However, individual Native Americans are United States citizens, and such are fully subject to the provisions of the Internal Revenue Code. Revenue Ruling 67-284, 1967-2 C.B. 55 states that there is no provision in the Internal Revenue Code of 1954 that exempts an individual from the payment of Federal income tax solely on the grounds that he/she is an Indian. Therefore, exemption of Indians from the payment of tax may only derive from treaties or agreements with the Indian tribes concerned, or some act of Congress dealing with their affairs. Although there are several sections of the Internal Revenue Code that exempt very limited types of income, to date the courts have not found any treaty language that exempts a Native American from taxation.

There are two specific types of land-related distributions made to members of Indian tribes that have been excluded by law. These are:

- Land claim settlement distributions under Title 25, Section 1402, and
- Income directly derived from restricted allotted lands.

Most of our questions come in relation to the second type.

Rev. Rul. 67-284, 1967-2 C.B. 55 gives us five tests to recognize the exempt status of income received by an enrolled member of an Indian tribe:

1. The land in question is held in trust by the United States Government
2. Land is restricted and allotted and is held for an individual noncompetent Indian, and not for a tribe
3. Income is derived directly from the land
4. Statute, treaty or other authority shows Congressional intent to protect the Indian until he/she becomes competent
5. Authority contains language indicating clear Congressional intent that the land, until conveyed in fee simple to the allottee, is not to be subject to taxation.

If one or more of these five tests is not met, and if the income is not otherwise exempt by law, it is subject to Federal income tax.

To help clarify, we must define some of the terms:

Trust Land: land owned by the federal government that has been set aside for the exclusive use of an Indian or tribe.

Fee Land: owned by a party outright. Also called deeded or patented land because someone holds a deed or patent to it.

Allotted Land: land that has been assigned by the federal government to an Indian.

Unallotted Land: land that has been assigned by the federal government to a tribe.

Rev. Rul. 56-342, C.B. 1956-2, 20, amplified by Rev. Rul. 62-16, C.B. 1962-1,7, provides initial guidance for "income derived from the land". Examples include; rentals (including crop rentals), royalties, sale of natural resources of the land, sale of crops grown upon the land, income from use of the land for grazing purposes, and income from the sale or exchange of cattle or other livestock raised on the land. Proceeds from the sale of restricted allotted land is exempt from tax per Rev. Rul. 57-407, C.B. 1957-2, 45.

Situation 1: Individual tribal member leases land from the tribe for farming, grazing, etc.

- Lease income received by the tribe is not taxable, but since the land is not allotted land, income is taxable to the individual.

Situation 2: Land belongs to another tribe member, held in trust; leased by an individual for farming

- Lease income received by the allottee is not taxable, but the income from farming is taxable to the leasee because the land is not his/her own allotment.

Situation 3: Land not held in trust

- Any transaction is taxable to all parties.



Student FICA Exception

In general, FICA tax applies to wages paid to an employee on account of employment. Section 3121(b)(10) excepts from FICA tax services performed in the employ of a school, college, university (SCU), or an affiliated section 509(a)(3) organization organized if the services are performed by a student who is enrolled and regularly attending classes at that institution. The student FICA exception does not apply to services which are covered by an agreement to provide social security coverage under Section 218 of the Social Security Act.

Effective April 1, 2005, Revenue Procedure 2005-11, 2005-2 I.R.B. 307 sets forth the generally applicable standards for determining whether services, performed by a student, in the employ of certain public or private nonprofit SCU, or section 509(a)(3) affiliated organizations qualify for the exception from FICA tax. The tests for determining eligibility for the student FICA exception are (1) whether the employer is a SCU and (2) whether the employee is a student.

An organization is not a SCU unless its "primary function" is to conduct educational activities. "Primary function" is the presentation of formal instruction, with a regular faculty and curriculum, and a regular enrolled body of students in attendance at a place where the educational activities are regularly carried on. The primary function requirement may cause the student FICA exception to be unavailable to certain organizations, such as hospitals and museums, that have embedded within them divisions or functions that carry on educational activities.

In order to have the status of a "student", an employee's services for the SCU must be incidental to and for the purpose of pursuing a course of study at the SCU. The educational aspect of the relationship must be dominant in order for the services to be incidental. Determining whether the services as an employee is incidental is determined separately each academic term. The educational aspect of an employee's relationship with the employer is generally evaluated based on the student/employee's course workload. A full-time student or half-time student qualifies for the student FICA exception. A half-time student means an enrolled student who is carrying at least a half-time academic workload at an institution of higher education, determined by that institution under its standards and practices.

A "full-time employee" is **ineligible** for the student FICA exception. Whether an employee is a full-time employee is based on the employer's standards and practices, except that an employee whose normal work schedule is 40 hours or more per week is always considered a full-time employee.

The student FICA exception is unavailable with respect to the services of a "professional employee". A professional employee is an employee whose work: (1) requires an advanced knowledge in the field of science or learning, (2) requires the consistent exercise of discretion and judgment, and (3) is predominantly intellectual and varied in character.

If the employee is eligible for employment benefits, he/she is not eligible for the student FICA exception because the eligibility for benefits generally suggests that an employee is not a student, instead they are a "career employee". A career employee is an employee who is eligible to participate in certain retirement plans, eligible for reduced tuition (with certain exceptions), or otherwise classified by the employer as a career employee.

The student FICA exception does not apply to services performed by an individual who is not enrolled in classes during school breaks of more than five weeks, including summer breaks of more than five weeks.

Question: Would a college student, employed at the college, qualify for the student FICA exception while working during the summer and not enrolled or attending any classes? **Answer:** No, because he/she is not enrolled and regularly attending classes. However, once school starts and he/she is enrolled and attending classes, he/she will be eligible for the student FICA exception for the time school is in session.

Mileage Rates Increase

In response to the recent gasoline price increases, the IRS and Treasury Department announced an increase in the optional standard mileage rates for the final four months of 2005. The rate will increase to **48.5 cents a mile** for all business miles driven from Sept. 1 through Dec. 31, 2005. This is an increase of 8 cents a mile from the 40.5 cent rate in effect for the first eight months of 2005, as set forth in Revenue Procedure 2004-64.

Federal Tax Calendar for Fourth Quarter 2005

October 2005

SUN	MON	TUE	WED	THU	FRI	SAT
						1
2	3	4	5 * make a deposit for 9/28-9/30	6	7 * make a deposit for 10/1-10/4	8
9	10	11 Employees earning tips in excess of \$20 in September must report amount to employer	12	13 * make a deposit for 10/5-10/7	14 * make a deposit for 10/8-10/11	15
16	17 ** Make a deposit for September if a monthly depositor	18	19 * make a deposit for 10/12-10/14	20	21 * make a deposit for 10/15-10/18	22
23	24	25	26 * make a deposit for 10/19-10/21	27	28 * make a deposit for 10/22-10/25	29
30	31					

November 2005

SUN	MON	TUE	WED	THU	FRI	SAT
		1	2 * make a deposit for 10/26-10/28	3	4 * make a deposit for 10/29-11/1	5
6	7	8	9 * make a deposit for 11/2-11/4	10 Employees earning tips in excess of \$20 in October must report amount to employer	11	12
13	14 * make a deposit for 11/5-11/8	15 ** Make a deposit for October if a monthly depositor	16 * make a deposit for 11/9-11/11	17	18 * make a deposit for 11/12-11/15	19
20	21	22	23 * make a deposit for 11/16-11/18	24	25	26
27	28 * make a deposit for 11/19-11/22	29	30 * make a deposit for 11/23-11/25			

*= Make a Payroll Deposit if you are under the semi-weekly deposit rule.

** = Make a Monthly Deposit if you qualify under that rule.

NOTE: Deposits made through EFTPS are due one day prior to the dates listed.

December 2005

SUN	MON	TUE	WED	THU	FRI	SAT
				1	2 * make a deposit for 11/26-11/29	3
4	5	6	7 * make a deposit for 11/30-12/2	8	9 * make a deposit for 12/3-12/6	10
11	12 Employees earning tips in excess of \$20 in November must report amount to employer	13	14 * make a deposit for 12/7-12/9	15 ** Make a deposit for November if a monthly depositor	16 * make a deposit for 12/10-12/13	17
18	19	20	21 * make a deposit for 12/14-12/16	22	23 * make a deposit for 12/17-12/20	24
25	26	27	28	29 * make a deposit for 12/21-12/23	30 * make a deposit for 12/24-12/27	31

*= Make a Payroll Deposit if you are under the semi-weekly deposit rule. NOTE: Deposits made through EFTPS are due one day prior to the dates listed.
 **= Make a Monthly Deposit if you qualify under that rule.

Return Filing Dates

October 31st

- > File Form 941 for the 3rd quarter of 2005. If all deposits paid on time and in full, file by November 10th.
- > File Form 730 and pay the tax on applicable wagers accepted during September.

November 30th

- > File Form 730 and pay the tax on applicable wagers accepted during October.

January 3, 2006

- > File Form 730 and pay the tax on applicable wagers accepted during November.

To add your name or e-mail address to our mailing list, please contact us via e-mail at Carole.M.Oller@irs.gov or call Carole Oller at (605) 787-5650