

ITG News
Keeping First Nations Informed

Publication 4267B
Catalog Number 37829B

Oklahoma Edition

April 2006

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Message from the Director

The recent Consultation Listening meeting held in February in Arlington, Virginia included a discussion on whether the Internal Revenue Service uses “cookies” to track access to www.irs.gov, the web site we use to provide all customers with ready access to federal tax information. While we reassured the attendees that there is no tracking of access and even posted a link at the bottom of the ITG landing page, the discussion made me realize that we should clearly articulate our overall concern for the privacy of Tribal tax information.

The Internal Revenue Code contains significant limitations on the accessibility of tax information. Quite simply, tax information is protected as some of the most confidential data that the federal government maintains. The IRS is prohibited from sharing information with very narrowly defined exceptions. Those exceptions generally cover court ordered releases, limited information sharing with other taxation agencies, and releases of information to Congress under federal statutes that require such information to be provided in order to enhance tax compliance.

The statutes impose severe penalties on any IRS official who releases information to a third party, whether orally or in writing, beyond those situations where it is a legal requirement, or necessitated to obtain necessary information for tax administration requirements. Such a situation might include sharing information with IRS Counsel where necessary to obtain legal advice on a Tribal issue.

Independent of the legal requirements that protect your tax information, I want to state my firm commitment to protecting the privacy of any conversations that you may have with me or my staff. For example, those who have attended the Consultation Listening meetings held to date are aware that we do not collect names of attendees unless they wish to provide them. Where Tribes have requested one-on-one meetings to discuss individual matters, we have scheduled them in a private area and have maintained those conversations as confidential.

We will continue to respect the requirements of federal law as well as respect your rights as a sovereign entity. Your information and our discussions will not be shared with anyone except those with a “need to know.”

As always, I am available to discuss any concerns you may have by calling me at (202) 283-9736.

Christie Jacobs

New Rules Outlined for ITIN Acceptance Agents

The Internal Revenue Service has announced new rules for individuals who participate in the Individual Taxpayer Identification Number (ITIN) Acceptance Agent program.

An Acceptance Agent is an individual, business or organization (college, financial institution, accounting firm, etc.) authorized by IRS to assist individuals in obtaining ITINs. Acceptance Agents review applicants' documentation, complete a certificate of accuracy, and forward the certificate and application to the IRS for processing.

The ITIN is for taxpayers who do not qualify for a Social Security Number but who still need the nine-digit identification number used by the IRS to process a Form 1040 and other tax schedules.

Revenue Procedure 2006-10 outlines the new rules and instructions for Acceptance Agents. The four major changes are:

- Acceptance Agent applicants are required to submit to suitability checks.
- Existing Acceptance Agent agreements will expire on December 31, 2006. Acceptance Agents must reapply to retain their approved status.
- Acceptance Agent agreements must be renewed every fourth year.

- Acceptance Agents may request their names be added to a publicly available list that will be published by the IRS.

These changes are part of an on-going IRS effort to ensure that ITINs are used strictly for tax administration purposes. In recent years, the IRS has made a number of revisions to the ITIN program such as requiring the ITIN application be accompanied by a completed tax form and streamlining the number of identification documents that Acceptance Agents can use to confirm the ITIN applicant's identity.

Form 13551, Application to Participate in the IRS Acceptance Agent Program, is available for printing or downloading from the IRS web site at www.irs.gov.

Employee Tip Income Program Questions

ITG has a full-time Tip Coordinator to assist you with any questions about tip reporting agreements. If you are interested in securing a Tip Agreement, have questions concerning your existing agreement, or have received a notice about tip reporting responsibilities that is unclear, please contact Julie Reese at (303) 231-5250, ext. 236.

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.

Common Compliance Problems Identified through Compliance Checks

Compliance Checks remain a valuable tool to assess the areas where tribes may have federal tax responsibilities and help to mitigate potential problems. Our January 2006 issue introduced the Tribal Evaluation of Filing and Accuracy Compliance (TEFAC) which was designed to allow qualifying tribes to conduct their own self Compliance Check. Information on the entire Compliance Check process, as well as useful references on common tribal tax issues, can be accessed on our web landing page by clicking on "Enhancing Federal Tax Compliance."

The following list shows the "Top 10" items that are surfacing via Compliance Checks and may be useful to you in assessing your own situation. If you believe you may have any of the issues outlined below, you may wish to

apply to conduct a self Compliance Check through our TEFAC program. The process is also outlined on our web site at www.irs.gov/tribes.

“The Top 10”

1. FUTA – tribes still making tax deposits and/or filing Forms 940 when they are not required to pay FUTA because they participate in State unemployment.
2. Noncompliance with Revenue Ruling 59-354 - Tribal council members' pay being handled incorrectly and reported on a Form 1099 instead of a Form W-2 or being reported on a Form W-2 with FICA, Medicare and income tax withheld.
3. Form 1099 problems:
 - the forms were not prepared at all,
 - the forms were prepared incorrectly (amounts in the wrong box, etc.),
 - the forms were prepared but not submitted to IRS,
 - the incorrect copy was submitted to IRS,
 - not aware of the exception to filing on payments to corporations,
 - not aware of requirement to file 1099 for medical and legal expenses, even if the recipient is incorporated.
4. Employment tax return filing/deposit problems
 - tax returns filed but no tax deposits were made,
 - deposits were made but no return was filed,
 - deposits were made to incorrect period,
 - deposits were made using the wrong timetable (e.g. monthly deposits when should be semiweekly),
 - unaware of the "next day" deposit rule,
 - Form 941 was filed with no Schedule B attached.
5. Forms W-9 and W-4 are not being used or are not being updated when necessary.
6. Unaware of requirement to backup withhold if no TIN provided prior to payment.
7. Payments to tribal members (committee members, gaming and non-gaming per capita) not reported on information returns, reported on the wrong information return, required withholding not done, or withholding done incorrectly.
8. Amounts on Forms W-2, W-3, and 941 don't reconcile.
9. Incorrect filing requirements for the entity, or there are other tribal entities that were not identified to the IRS as belonging to the tribe.
10. Unaware of magnetic media filing requirement, and unaware of FIRE system (Filing Information Returns Electronically).

Addressing Your Feedback

Many tribes have taken the time to tell us how we can better serve their federal

tax administration needs. Participation by Tribes in the annual ITG Customer Satisfaction Survey, Consultation Listening meetings, and direct contacts, has enabled us to identify areas where we can improve the products and services that we provide for tribes while still maintaining those that are valued as they currently exist.

Below are some changes that are currently being implemented as a result of your feedback. Other changes will soon follow:

- As new federal tax developments surface, we will be using our tribal e-mail distribution list to send information directly to you in a more timely manner.
- A headline area of our web site landing page will now focus on "Recent Developments" and will provide a direct link to recent court cases, new IRS Counsel rulings and opinions, updated ITG web site postings, new ITG products, and newly enacted federal tax legislation that could impact tribes.
- We will be creating a "Helpful Hints to Avoid Penalties" guide to post on the ITG web site along with a blast e-mail distribution showing a link to that new guide.
- With your assistance, we will undertake a structured canvass to identify issues that are unique to your Tribe.
- At a minimum, we will notify tribes annually of the name and telephone number of their assigned ITG Specialist.

ITG is committed to meeting your needs as they are identified. Since the annual IRS Satisfaction Survey is the primary mechanism to assist us in determining areas for improvement, we want to encourage your participation in the survey. It will be mailed to you in late-summer 2006.

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.

Recent Ruling Addresses Schemes Targeting American Indians

The IRS has warned, in a ruling released March 16, 2006 (Rev. Rul. 2006-20), individuals, promoters, and return preparers against seeking to avoid tax

liabilities by claiming an exemption from federal income tax for American Indians under an unspecified "Native American Treaty." The IRS says it has become aware of marketing schemes that make that frivolous argument.

The Service is aware that some taxpayers are attempting to reduce their federal tax liability by claiming tax exempt status based on a general "Native American Treaty." The Service is also aware that some promoters, including return preparers, are advising or recommending that Native American taxpayers take the frivolous position that they are exempt from federal income tax based on an unspecified Native American treaty. Some promoters market a package, kit or other materials that claim to show taxpayers how they can avoid paying income taxes based on these and other meritless arguments.

This revenue ruling emphasizes to taxpayers, promoters, and return preparers that there is no right to exemption from federal income tax for Native Americans under an unspecified "Native American Treaty." Any return position based on an unspecified "Native American Treaty" has no merit and is frivolous. As a general rule, Native Americans are subject to federal income tax just like every other American.

The Service is committed to identifying taxpayers who attempt to avoid their federal tax obligations by taking frivolous positions. The Service will take vigorous enforcement action against these taxpayers and against promoters and return preparers who assist taxpayers in taking these frivolous positions. Frivolous returns and other similar documents submitted to the Service are processed through the Service's Frivolous Return Program. As part of this program, the Service confirms whether taxpayers who take frivolous positions have filed all of their required tax returns, computes the correct amount of tax and interest due, and determines whether civil or criminal penalties should apply. The Service also determines whether civil or criminal penalties should apply to return preparers, promoters, and others who assist taxpayers in taking frivolous positions, and recommends whether an injunction should be sought to halt these activities. Other information about frivolous tax positions is available on the Service website at www.irs.gov.

ISSUE

Whether taxpayers may avoid their federal income tax liability by claiming tax exempt status based on an unspecified "Native American Treaty."

FACTS

Taxpayer A is a Native American and receives income from a tribal or non-tribal source. The income paid to taxpayer A is reported on an information return (e.g., a Form 1099-MISC, Form W-2. etc.). Taxpayer A then either: 1) fails to report the income shown on the information return on his federal income tax return, claiming an erroneous exemption from federal income tax under an unspecified

"Native American Treaty," or 2) wrongly reports a loss offsetting the information return income on the "Other Income" line of his federal income tax return with an explanation that reads, "Less - Native American Treaty" or "Native American Treaty."

LAW AND ANALYSIS

Native Americans are subject to the same income tax laws as other U.S. citizens unless there is an exemption explicitly created by treaty or statute. *Squire v. Capoeman*, 351 U.S. 1, 6 (1956); *Estate of Poletti v. Commissioner*, 99 T.C. 554, 557-58 (1992), *aff'd*, 34 F.3d 742 (9th Cir. 1994); *Doxtator v. Commissioner*, T.C. Memo. 2005-113. Any exemption must be based on clear and unambiguous treaty or statutory language. *Squire*, 351 U.S. at 6; *Ramsey v. United States* 302 F.3d 1074 (9th Cir. 2002); *Cook v. United States*, 86 F.3d 1095 (Fed. Cir. 1996); *Estate of Peterson v. Commissioner*, 90 T.C. 249, 250 (1988). Under the Internal Revenue Code, all individuals, including Native Americans, are subject to federal income tax. Section 1 imposes a tax on all taxable income. Section 61 provides that gross income includes all income from whatever source derived. Adjustments to income, deductions, and credits must be claimed in accordance with the provisions of the Internal Revenue Code and accompanying Treasury regulations. Although there are certain exemptions and other provisions throughout the Internal Revenue Code that apply to Native Americans, none of these exempt individual Native American taxpayers from federal tax. Moreover, under the Indian Gaming Regulatory Act, any distribution of casino gaming proceeds to individual tribe members is also subject to federal income tax.

Additionally, while there are numerous valid treaties between various Federally Recognized Indian Tribal Governments and the United States government, some of which may contain language providing for narrowly defined tax exemptions, these treaties have limited application to specific tribes. Any exemptions from federal tax are expressly stated in the language of the treaty. Taxpayers who are affected by such treaty language must be a member of a particular tribe having a treaty and must cite that specific treaty in claiming any exemption. There is no general treaty that is applicable to all Native Americans.

HOLDING

Taxpayer A made improper and unfounded claims for exemption from federal income tax by either failing to report his income or reporting it and claiming an offsetting deduction. Any claim that a taxpayer is exempt from federal income tax due to a general "Native American Treaty" is frivolous. Unless a taxpayer can cite a specific treaty or statutory language providing for exemption of income from federal income tax, that taxpayer is subject to all applicable federal income tax laws. Thus, Taxpayer A must report the income shown on the information return and may not report a loss or exemption attributable to a general Native American treaty to offset the income received from the tribal organization.

CIVIL AND CRIMINAL PENALTIES

The Service will challenge the claims of individuals who attempt to avoid or evade their federal tax liability. In addition to liability for the tax due plus statutory interest, taxpayers who fail to file valid returns or pay tax based on the argument that they are exempt from income tax due to a general "Native American Treaty" face substantial civil and criminal penalties. Potentially applicable civil penalties include: (1) the section 6662 accuracy-related penalties, which are generally equal to 20 percent of the amount of taxes the taxpayer should have paid; (2) the section 6663 penalty for civil fraud, which is equal to 75 percent of the amount of taxes the taxpayer should have paid; (3) a \$ 500 penalty imposed under section 6702 when the taxpayer files a document that purports to be a return but that contains a frivolous position or suggests a desire by the taxpayer to delay or impede the administration of federal income tax laws; (4) the section 6651 additions to tax for failure to file a return, failure to pay the tax owed, and fraudulent failure to file a return; and (5) a penalty of up to \$ 25,000 under section 6673 if the taxpayer makes frivolous arguments in the United States Tax Court.

Taxpayers relying on these frivolous positions also may face criminal prosecution under: (1) section 7201 for attempting to evade or defeat tax, the penalty for which is a significant fine and imprisonment for up to 5 years; (2) section 7203 for willful failure to file a return under, the penalty for which is a significant fine and imprisonment for up to 1 year; and (3) section 7206 for making false statements on a return, statement, or other document, the penalty for which is a significant fine and imprisonment for up to 3 years.

Persons, including return preparers, who promote these frivolous positions and those who assist taxpayers in claiming tax benefits based on frivolous positions may face civil and criminal penalties and also may be enjoined by a court pursuant to sections 7407 and 7408. Potential penalties include: (1) a \$ 250 penalty under section 6694 for each return or claim for refund prepared by an income tax return preparer who knew or should have known that the taxpayer's position was frivolous (or \$ 1,000 for each return or claim for refund if the return preparer's actions were willful, intentional or reckless); (2) a penalty of up to \$ 1,000 under section 6700 for promoting abusive tax shelters; (3) a \$ 1,000 penalty under section 6701 for aiding and abetting the understatement of tax; and (4) criminal prosecution under section 7206, resulting in a significant fine and imprisonment for up to 3 years, for assisting or advising about the preparation of a false return statement or other document under the internal revenue laws.

Federal Tax Calendar for Second Quarter 2006

April 2006

- | | |
|---------------------|--|
| Wednesday, April 5 | - * make a deposit for 3/29-3/31 |
| Friday, April 7 | - * make a deposit for 4/1-4/4 |
| Monday, April 10 | - employees report March tip income to employers if \$20 or more |
| Wednesday, April 12 | - * make a deposit for 4/5-4/7 |
| Friday, April 14 | - * make a deposit for 4/8-4/11 |
| Monday, April 17 | - **make a deposit for March if under the monthly Deposit Rule |
| Wednesday, April 19 | - *make a deposit for 4/12-4/14 |
| Friday, April 21 | - *make a deposit for 4/15-4/18 |

May 2006

- | | |
|-------------------|--|
| Wednesday, May 3 | - *make a deposit for 4/26-4/28 |
| Friday, May 5 | - *make a deposit for 4/29-5/2 |
| Wednesday, May 10 | - *make a deposit for 5/3-5/5 |
| | - employees report April tip income to employers if \$20 or more |
| Friday, May 12 | - *make a deposit for 5/6-5/9 |
| Monday, May 15 | - **make a deposit for April if under the monthly deposit rule |
| Wednesday, May 17 | - *make a deposit for 5/10-5/12 |
| Friday, May 19 | - *make a deposit for 5/13-5/16 |
| Wednesday, May 24 | - *make a deposit for 5/17-5/19 |
| Friday, May 26 | - *make a deposit for 5/20-5/23 |

June 2006

- | | |
|--------------------|--|
| Thursday, June 1 | - *make a deposit for 5/24-5/26 |
| Friday, June 2 | - *make a deposit for 5/27-5/30 |
| Wednesday, June 7 | - *make a deposit for 5/31-6/2 |
| Friday, June 9 | - *make a deposit for 6/3-6/6 |
| Monday, June 12 | - employees report May tip income to employers if \$20 or more |
| Wednesday, June 14 | - *make a deposit for 6/7-6/9 |
| Thursday, June 15 | - **make a deposit for May if under the monthly deposit rule |
| Friday, June 16 | - *make a deposit for 6/10-6/13 |
| Wednesday, June 21 | - *make a deposit for 6/14-6/16 |
| Friday, June 23 | - *make a deposit for 6/17-6/20 |
| Wednesday, June 28 | - *make a deposit for 6/21-6/23 |
| Friday, June 30 | - *make a deposit for 6/24-6/27 |

* 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 must be initiated at least one day prior to the due dates listed above in order to be timely.

Return Filing Dates

May 1st

- File Form 730 and pay the tax on applicable wagers accepted during March.
- File Form 941 for the 1st quarter of 2006. If all deposits paid on time and in full, file by May 10th.

May 31st

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

June 30th

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