

Revenue Ruling 68-38

SECTION 3402. - INCOME TAX COLLECTED AT SOURCE

26 CFR 31.3402(a)-1: Requirement of withholding.

(Also Sections 61, 3121, 3306, 3401; 1.61-2, 31.3121(a)-1, 31.3306(b)-1, 31.3401(a)-1.)

1968-1 Cumulative Bulletin 446. Revenue Ruling 68-38

January, 1968

Payments made from funds provided under both Title II-A of the Economic Opportunity Act of 1964 and the Manpower Development and Training Act of 1962 to unemployed and underemployed residents of an Indian reservation who participate in a training program to acquire skills in the construction trades are not "wages" subject to the Federal employment taxes, including income tax withholding. Furthermore, such payments fall in the same category as other unemployment relief payments and are not compensation for services includable in the gross incomes of the enrollees.

Advice has been requested by an Indian tribal council regarding the status, for purposes of the Federal Insurance Contributions Act, the Federal Unemployment Tax Act, and the "Collection of Income Tax at Source on Wages" (chapters 21, 23, and 24, respectively, subtitle C, Internal Revenue Code of 1954), of payments made to enrollees participating in a training program established under Title II-A of the Economic Opportunity Act of 1964, Public Law 88-452, 42 U.S.C. 2701.

The training program is part of a community action project being conducted on an Indian reservation to train unemployed and underemployed residents of the reservation in the field of construction trades skills so that they can obtain regular work in the home construction industry on and off the reservation. The Indian tribal council sponsors the program, controls its conduct and administration, and provides the training materials. The program, which is of twelve-month duration, is funded by both the Office of Economic Opportunity (OEO) and by the Department of Labor under the Manpower Development and Training Act (MDTA) of 1962, 76 Stat. 23-33. During the first three months, the enrollees receive \$50 per week paid by the tribal council's community action project director from funds furnished by the OEO. During the remaining nine months, the enrollees receive amounts ranging from \$41 to \$61 per week which are paid by the unemployment agency of the State in which the project is located from funds allotted to it under the MDTA. These amounts are based on the unemployment compensation rates in the State, the variance depending upon the number of dependents of the enrollee.

The operation of the program is under the direction of a supervisor and several instructors in carpentry, masonry, electricity, plumbing, 447 and sheet metal heating. In order to participate in the program an enrollee must be at least 21 years of age and must be the head of a household. Each enrollee is trained in subject matter, work habits, and performance by a full-time instructor and is under close supervision at all times. An enrollee may be dismissed for inability to learn or unwillingness to adhere to the program's standards. Dismissal is based on the recommendation of the instructor with the approval of the program supervisor and the project director.

Because it is believed that the enrollees learn more quickly and thoroughly by participating in actual home construction, the twelve-month program includes the construction of new homes as well as repairs on various public buildings and facilities. In addition to this on-site training, indoor classes covering managerial and administrative work are conducted and are scheduled so as to fall as much as possible within bad weather periods. However, class work is continually interspersed so that there is a constant learning progression. Each enrollee's time is divided on a substantially equal basis into three areas, which include, (1) classroom training; (2) demonstration, [*4] work on mock-ups, practice drill; and (3) new unit construction.

Indian tribal councils are responsible for the withholding of Federal employment taxes where applicable and for the payment of any employer taxes owing with respect to "wages" paid to their employees (other than council members). See Revenue Ruling 59-354, Cumulative Bulletin 1959-2, 24. The primary question in this case is whether the payments made to the enrollees by the tribal council are "wages" for services performed by them as employees.

In general, the purpose of programs funded by the MDTA is to aid unemployed and underemployed individuals to obtain better employment opportunities upon completion of their training. This may be accomplished by either an institutional-type educational and training program in which employment is not involved, or by an on-the-job training program in which an unemployed individual is placed with an employer and the employer is required to pay him not less than the minimum wage. As indicated in Revenue Ruling 63-136, Cumulative Bulletin 1963-2, 19, the MDTA, in addition to providing benefits to individuals participating in the institutional-type programs, also authorizes the payment of benefits to persons undergoing on-the-job training. However, under the provisions of the Act, the amount of any payment which would otherwise be made to such a person is reduced by an amount which bears the same ratio to the payment as the number of compensated hours per week bears to forty hours. Revenue Ruling 63-136 holds that benefit payments made under the MDTA fall in the same category as other unemployment relief payments made for the promotion of the general welfare and are not includable in the gross incomes of the recipients.

In the instant case, the training program is primarily of the institutional training-type insofar as the MDTA is concerned. Except for the source and manner of payments made during the period financed by funds from the OEO, there is no significant difference in the training situations between the two periods of the year. The basic purpose of the program, insofar as the enrollees are concerned, is to train them during a twelve-month period, and an employment relation is neither intended nor established. Accordingly, the enrollees are not employees for purposes of the Federal employment taxes, including income tax withholding, and the payments received by them are not "wages" subject to those taxes.

Moreover, since the basic purpose of the training program, which is funded by both the OEO and the MDTA, is to train unemployed and underemployed residents of the reservation in the field of construction trades skills so they can obtain regular work in the home construction industry on and off the reservation, the payments fall in the same category as the payments covered in Revenue Ruling 63-136 and are not compensation for services includable in the gross incomes of the enrollees, for Federal income tax purposes.