




Foreign Nationals Tax Compliance Program

Accounts Payable Training for NCAS State Agencies


April 18, 2012



Disclaimer

- The information within this presentation does not constitute tax/legal advice and each agency should seek his/her own counsel in addressing specific situations. The NC Office of the State Controller is providing this training as a way of enhancing the knowledge of the participants who are implementing and maintaining the Foreign Nationals Program within their agency. Information presented is not intended to be used for the purpose of avoiding any penalties that may be imposed on the taxpayer by any taxing authority or agency.
- Any questions that are not handled within the presentation will be responded to via email. Further follow-up questions can be submitted to Jennifer Trivette, with the NC Office of the State Controller, at jennifer.trivette@osc.nc.gov.


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Panelist

- Jennifer Trivette, Risk Mitigation Analyst
 - NC Office of the State Controller
- Clayton Darnell, OSC SAD NCAS Model Team
 - NC Office of the State Controller
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 - NC Office of the State Controller

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Agenda

- Challenges
- U.S. or Non U.S. Person
- Form W-9 Solicitation rules
- TINs and Withholding
- Documenting Non U.S. Status
- Presumption Rules
- Best Practices


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Foreign National Challenges

- Establishing Effective Policies and Procedures to comply with government requirements
 - Gathering information to comply with rules
 - Timely communicating changes in data that impact compliance
 - Keeping current in government rules and procedures
 - Balancing knowing both immigration laws and tax laws


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Foreign National Challenges


- Best practices in making payment to Nonresident Aliens (NRAs)
 - Implement policies and procedures for meeting IRS due diligence.
 - Recommend posting them to your website
 - Keep up-to-date on rules and forms procedures –they change frequently!

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Policy 


- The reporting and withholding of taxes associated with payments made to NON-U.S. citizens by universities, community colleges, and other agencies of the State of North Carolina are in accordance with the laws and regulations of the U.S. Citizenship and Immigration Services and the Internal Revenue Services.

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Policy 


- The U.S. Citizenship and Immigration Services define what payments may be made to aliens who perform services in the United States.
- The Internal Revenue Service defines which payments made to aliens are reported and subject to taxes, as well as establishes the tax rate for those payments.

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U.S. or Non U.S. Person? 

- Two primary tax categories of payees
 - U.S.
 - Non U.S.
- Tax documentation, reporting and withholding rules differ depending on who your payee is for tax purposes.
- Tax status has little to do with citizenship
 - Except that U.S. citizenship will control.
 - If payee is not a U.S. citizen, then you must determine the payee's country of tax residency.


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U.S. or Non U.S. Person?

- U.S. Persons
 - Subject to U.S. tax on their worldwide income.
- Non U.S. Persons
 - Note that many foreign nationals believe that, because they are not U.S. citizens, but are citizens of another country, they are not/cannot be subject to U.S. tax (FALSE).
 - However, foreign nationals who are not U.S. tax residents (non U.S. persons) are subject to U.S. tax on their U.S. source income. (U.S. Source Income)
 - Non U.S. source income paid to a non U.S. person is not subject to reporting or withholding. (Foreign Source Income)
 - But must document payee's non U.S. status to apply this rule.


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A Note on the Word "Person"

- "Person" includes individuals, as well as entities.
- For example, ABC Corporation is a corporation organized under the laws of North Carolina.
- ABC Corporation is a U.S. Person for tax purposes.


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U.S. vs. Non U.S.

<ul style="list-style-type: none"> • U.S. • WORLDWIDE INCOME <ul style="list-style-type: none"> - Citizens - Residents <ul style="list-style-type: none"> • Green card • Substantial Presence test (SPT) - Entities Organized under U.S. Law <ul style="list-style-type: none"> • W-9/1099 <ul style="list-style-type: none"> • 28% backup withholding • Some corporation exemptions • \$600 threshold for most reporting - No treaty benefits (some exceptions) - Filing deadlines <ul style="list-style-type: none"> • Payees: 1/31 • IRS: 2/28-4/30 	<ul style="list-style-type: none"> • Non U.S. • U.S. Source Income <ul style="list-style-type: none"> - Not U.S. Citizens or resident s - Not organized under U.S. law <ul style="list-style-type: none"> • W-8s/8233/1042-S <ul style="list-style-type: none"> • 30% withholding • 4% NC State (if applicable) • No corporate exemption • No minimum dollar threshold for payments - Can claim treaty benefits to avoid or lessen U.S. taxation/ withholding if qualify - Filing deadlines <ul style="list-style-type: none"> • Payees - Form 1042-S: 3/15 • IRS - Form 1042-S: 3/15-4/15
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Documentation

- U.S. Persons
 - Form W-4
 - Form W-9
- Non U.S. Persons
 - Form W-4
 - Form W-8BEN, -ECI, -IMY, -EXP, -CE
 - 8233 - Exemption From Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual


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Rules for Sourcing Income

- A determination is made as to the source of income in the following manner:
 - Compensation paid to employees and independent contractors, income is sourced to the country where services are performed.
 - For non compensation – non-payments such as scholarships/fellowships, grants, prizes and awards, the source of income is the residence of the payor regardless of who actually disburses the funds.


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Rules for Sourcing Income

- Royalties
 - Based on where the property is used
 - Keep separate records for property used both within and without the U.S.
 - Avoids having to withhold on total income
 - Must differentiate between
 - Payment for use of intangible property (royalties)
 - Payment for creating intangible property (services)
 - Sale of all substantial rights in intangible property (sale proceeds)


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Rules for Sourcing Income

- **Resident Alien** – follows the same withholding tax rules as U.S. Citizens. The federal withholding rates for resident aliens are the same as rates for U.S. Citizens.
- **Non-resident Alien** – all U.S. sourced income is taxable with a few exceptions.
 - Federal Tax Rate 14%-30%
 - NC Tax Rate 4% – Contractors with ITINs
 - NRAs wages are also subject to 4 step gross up process (formerly known as the ARRA)
 - Tax Treaties


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Rules for Withholding

- No W/H certificate is required if no withholding tax reduction is claimed
- Best to collect
 - Form W-9 as a certificate of U.S. status
 - Form W-8BEN as a certificate of foreign status
 - Not needed for scholarship/fellowship grants for qualifying F, J, and M students taxed at 14%


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Rules for Withholding

- Withholding certificates for a withholding tax exemption
 - Form 8233 for compensation for personal services
 - Form W-9 for RA exempt for tax under a treaty
 - Form W-8ECI for effectively connected income
 - But cannot be used for compensation for personal services
 - Form W-8EXP for income of a tax-exempt entity
 - Form W-8BEN for all other U.S. income.


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Rules for Withholding

- Withhold at the highest rate if
 - The documentation is unreliable
 - Documentation is not provided
 - Except can withhold 14% on grants paid to those in qualifying F, M, J, or Q Status based on presumptions
 - You know or have reason to know that the actual rate is higher than the rate supported by documentation provided.


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Presumptions

- Generally, all payees are presumed to be U.S. persons.
 - Therefore, subject to U.S. tax on worldwide income.
 - Subject to form 1099 reporting and 28% backup withholding regardless of where in the world located.
 - To remove them from the application of worldwide taxation and subject them to reporting and withholding only on payments of U.S. source income, you must obtain from them documentation of their non U.S. Status.
 - For example: Form W-8 or 8233


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Presumptions

- This presumption is why you must obtain documentation from you payee that they are non U.S. persons.
 - You are asking them to document a negative, essentially (that they are not something).
 - You also need to navigate, possibly, the culturally sensitive and political responses to this presumption.


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Presumptions

- You must ask for this documentation even if you know that you are paying non U.S. source income.
- Why?
 - Because you cannot get to the point where you apply U.S. tax only against U.S. source income until you first document that your payee is on the "right-hand" side.


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Form W-9 Solicitation Rules

- If your payee is a U.S. person, unless there is an exception, you must obtain a Form W-9, or applicable substitute, from them for tax reporting purposes.

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Exceptions to Form W-9 Solicitation Requirements

- IRS "Eyeball" Test
 - Tax-exempt entities
 - Government payees

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“Eyeball” Test and Corporations

- Currently, the IRS does allow use of the “eyeball” test for corporate payees.
- If the payee has clear indication of corporate status in its name, you can exempt if from 1099 reporting without obtaining a Form W-9.
 - Inc., P.C., Corp., etc.
- CAUTION:
 - You must know for certain that your payee is a U.S. person.
 - No corporate exemption from the Form 1042-S reporting and withholding rules for foreign corporations.
 - Advice: avoid using “eyeball” test for corporations.
 - No minimum dollar threshold for payments

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Goods Purchases


- Currently, purchases of goods are exempt from Form 1099 (and 1042-S) reporting.
- If you are purchasing only goods, no withholding certificate (W-9, W-8, etc.) is required until 2012.
- But watch for warranty payments and interest charges on installment purchases, or late fees.
 - These payments are reportable and subject to withholding rules.

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TINs and Withholding


- For Form 1099 reporting purposes, you must obtain the payee's TIN if making a reportable payment to avoid having to withholding 28% in federal income taxes from the payment.
- For Form 1042-S reporting purposes, the only way to avoid the 30% withholding requirement is:
 - Payment of non U.S. source income to non U.S. person;
 - Valid claim by payee that payment is one of effectively connected income;
 - Valid treaty claim.
 - Note that some treaties still require some withholding.
 - Therefore, your non U.S. person payee may have a U.S. TIN, and you may still be required to withhold.

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Use Form W-8BEN to Document Payee's Non U.S. Status 


- Payee must complete at least lines 1 through 4
- Signature, date and capacity lines at bottom.

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Form W-8BEN 

- Having the Form W-8BEN substantiates payee's status as non U.S. person payee.
- Then, if you are paying non U.S. source income, no reporting or withholding is required.
 - You must also document that the income is non U.S. source
 - Contract, Invoice, correspondence, bills of lading, etc.

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Form W-8BEN 


- You may be required/asked to explain to your non U.S. payees why you need U.S. Tax documentation from them.

The Answers:

 - Because the U.S. taxes its residents on their worldwide income.
 - To avoid U.S. tax withholding on non U.S. source income, they must document for you, as a U.S. payor, their non U.S. Status.

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Form W-8BEN



- Can be used:
 - Solely to document non U.S. status
 - Individual or entity
 - To claim treaty benefits on passive investment income
 - Entity or individual
 - U.S. TIN required, except for dividends
 - To claim treaty benefits on services
 - If payee not claiming ECI
 - Entity only – not individuals
 - U.S. TIN REQUIRED!!!!
 - Individual payees claiming treaty benefits on payments for services do so using the Form 8233.

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Best Practices



- Best answer for domestic A/P process: All U.S. individuals and U.S. entities, particularly those with "Presumptions of Foreign Status" should provide a W-9 to avoid exposure for NRA withholding and to give 1099 reporting or exemption information.
- This method is the simplest and easiest to build procedures around a policy that requires documentation from all payees.
- Where no document is received, follow the presumption standards mentioned earlier.


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Best Practices




- Foreign-source compensation
 - No documentation needed if:
 - All the services are performed outside the U.S.
 - No reason to know that the individual is a U.S. citizen or resident alien, and
 - The income is not effectively connected with a U.S. trade or business.
 - Best to collect a Form W-8BEN as a certificate of foreign status (no TIN required) and include location of services in the contract and payment requests.

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Best Practices


- A policy requiring a W-9 from all U.S. entities even if an exempt recipient through the "eyeball test" would flush out the reportable entities.

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Documentation - REQUIRED

- Required if:
 - Services are performed in the states (keep evidence for audit purposes)
 - Employer has reason to know worker is a
 - United States Citizen
 - Lawful Permanent Resident, or
 - Resident Alien
 - Services are effectively connected to a U.S. trade or business
- Best Practice: Collect for W-8BEN (signed original) and invoice/purchase order and send copies to State Controller's Foreign National Team
OSC.Foreign.National.Team@osc.nc.gov


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Who Makes the Determination Whether Income is Subject to Withholding?

- In order to apply the right tax treatment, A/P and not the payee needs to determine:
 - What type of income is being paid
 - The sourcing and it will vary by income type
 - Taxability
 - The rate of withholding
 - If compensation, whether payment is for independent or dependent services
 - Treaty benefits applicable
- IRS deems this to be an important point.

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Heat Ticket –



OSC Support Services
- 919-707-0795
- E-Mail:
OSC.Support.Services@os.c.nc.gov

Message
Microsoft E-mail Scan

You forwarded this message on 4/16/2012 12:30 PM.
From: heat@os.c.nc.gov
To: OSC Foreign Nationals Team
Cc: Vendor
Subject: Vendor

Name: Jane Smith / Operator ID: 24444
Phone: (919) 707-0795


Call Description: Chestina is wanting to add:
YES LOGIC PTY LTD
7/39 BOULVERIE ST
CARLTON VIC, VI 3053

See attached for WS-BEN form.
Ticket #: 00275996
Entered by: jwoosten
Region: P
Agency: 02 - Administrative Office of the Courts


Ticket information below.
Please change to working, assign, acknowledge, and save this ticket.

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Deposit Requirements:




Training Video -
http://www.ncosc.net/Foreign_Nationals/Foreign_Nationals_Training.html




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Deposit Requirements:



U.S. SOURCE WITHHOLDING ON FOREIGN PERSONS	
Amount of Deposit (Withholding)	IRS Deposit Requirements
Less than \$200	Annually with 1042T filing (Due March 15)
Between \$200 and Less than \$2,000	Within 15 days after the end of the month
\$2,000 or greater	Within 3 banking days

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NCAS Demo


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Contact Information

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THANK YOU!

Source: COKALA Tax information Reporting Solutions, LLC.
Windstar Technologies, Inc.
IRS Publication 515
NC Office of State Controller Website

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