




FOREIGN NATIONALS TAX COMPLIANCE TRAINING

“Improving Efficiencies and Effectiveness of Your Foreign Nationals Tax Compliance Program and Current Issues Update”

October 14th, 2015




Presenters

- **Jennifer Pacheco**, Foreign Nationals Tax Compliance Program
 - NC Office of the State Controller

Disclaimer: The information within this presentation does not constitute tax/legal advice and each participant should seek his/her own counsel in addressing specific situations.


2



Training Agenda

- Review Factors to Process Payments
- Requirements of Paying a Foreign National
- Review of Forms
- Preparing for Year-End – Reviewing your Foreign National (Audit) File
- Regulation Updates/Awareness of Current Issues


3



Factors of Payment

- **Who are you paying?**
 - Individual or Entity
 - Who is the beneficial owner of the income
 - No assignments
 - Determine cash value for "in-kind" items
 - Payments to Foreign Performers
 - Agent for the Foreign National – CWA Required for tax exception
 - Agent's fee is not excluded from performers income
- **What are you purchasing?**
 - Terminology has no tax implication
 - What are the conditions of the payment?
 - Is there a contract?
 - Does the contract address tax withholding and immigration documents?
 - Location of services being performed?
 - Is there a taxable and non-taxable portion of the contract?
 - Have you been invoiced?


4



Factors of Payment (cont.)

- **What is the source of the payment?**
 - U.S. Source
 - Foreign Source
 - What is the foreign liability in country of where services are performed?
 - Liability of activities being performed for your institution?
- **Who is eligible to perform services?**
- **What is the Tax Status (SPT)**
- **How is payment being processed?**
 - HR System
 - Student Financials
 - Accounting


5



Requirements of Paying a Foreign National


- **All compensation for services performed in the United States is subject to taxation unless an exception applies**
 - **What are these EXCEPTIONS**
 - Tax Treaties – with a few examples
 - Statutory/Reduced Taxation – Rates (5%, 14%, 30%)
 - Maximum Amounts – First \$5,000 is exempt from tax.
 - Elimination of Tax withholding in U.S. – Business Profit Articles
 - **Note that being exempt from withholding does not mean exempt from reporting, nor does it mean the income excludable from the beneficial owner's gross income for tax return purposes. It also does not mean it isn't taxable income to the beneficial owner.**

6

Requirements of Paying a Foreign National (cont.) 

- Taxation depends on his or her U.S. tax status – resident alien or nonresident alien for tax purposes
 - Resident Aliens and U.S. Citizens
 - Taxed on their Worldwide Income
 - Nonresident Aliens
 - Taxed on their U.S. Source Income

7


Requirements of Paying a Foreign National (cont.) 

Thinking Outside the BOX!!!

- Taxation depends on U.S. tax status –
 - You have a foreign student, F-1 status that is in resident alien tax status. The student will be returning to their home country of Spain to finish out their degree doing research, during the months of November and December, while being paid for their research.

What is the character of this income and is it Reportable?

8

Requirements of Paying a Foreign National (cont.) 

- U.S tax residency status depends on his or her U.S. immigration status and U.S. presence over a 3-calendar year period.
 - Substantial Presence Test
 - Current Immigration Status
 - Primary Purpose of Presence
 - Date of Arrival
 - Any prior dates of Arrival
 - Important – Define for your agency how you will gather this information and maintain this information.

9

Requirements of Paying a Foreign National (cont.) 


- A resident alien, like a U.S. Citizen is subject to U.S. tax on worldwide income, even if the individual resides and works abroad, unless an exception applies.

Coca-Cola may owe \$3.3 billion in extra taxes




Source: <http://fortune.com/2015/09/18/coca-cola-taxes-irs/>

10

Requirements of Paying a Foreign National (cont.) 


- A nonresident alien is subject to U.S. taxation on U.S. source income and income effectively connected to the conduct of a U.S. trade or business (ECI), unless an exception applies.
 - Collect W-8ECI (Require - US TIN)
 - Exempt Taxation
 - Report Income on 1042-S

11

Requirements of Paying a Foreign National (cont.) 


- All payments made by an employer to or on behalf of an employee, including cash and the FMV of benefits-in-kind, are wages subject to payroll taxes, unless an exception applies.
 - Are services required to receive payment?
 - Exempt based on Substantial Presence Test
 - (FICA)
 - Exempt/Reduced based on Tax Treaty

12

Requirements of Paying a Foreign National (cont.) 


- Document the exception by submitting a completed form, signed under the penalties of perjury, to the employer or payer, otherwise the exception does not apply.
 - W-8 Forms must include specific treaty exemption to exempt the taxes.
 - Royalties
 - Business Profit Articles

13

Requirements of Paying a Foreign National (cont.) 


- The IRS enforces withholding by collecting the tax, plus penalties and interest, from the payer who fails to withhold or to collect the necessary form for the exemption from withholding.

14

Forms 

- **W-8BEN**
 - Only for individuals
 - Requires a foreign taxpayer identification number or date of birth (identification purposes in information exchange).
 - Request country of citizenship (this may not be the same as country of residence for treaty benefits).
- **Changes to form**
 - Part 1
 - Line 2 – Country of Citizenship
 - Line 3– Type of Beneficial Owner – Removed
 - Line 6 – Foreign TIN – No longer states Optional
 - Line 9 – Date of Birth
 - Part 2
 - Simplified
 - Signature line
 - Print name of Signer


15



Forms (cont.)

- **W-8BEN-E**
 - Only for Entities
 - 8 pages
- **Some highlights**
 - Part 1
 - Line 5 – FATCA Status (31 boxes)
 - Not Required if not a FATCA payment
 - Line 8/9 – US TIN and/or Foreign TIN
 - Part 3
 - Similar to Treaty in former W-8BEN
 - Signature line
 - Print name of Signer
 - Check box certify authority to sign
- **Please read directions for all details of W-8BEN-E**


16



Forms (cont.)

- **W-8ECI**
 - Serves to exempt the payment from withholding
 - EXCEPTION – N/A for independent personal services or income paid to a personal holding company.
- **Changes to form**
 - Part 1
 - Line 2 – Country of residence for tax purposes
 - Line 5 – Permanent residence (same as line 2)
 - Line 7 – U.S. TIN – required
 - Line 8 – Foreign TIN – no longer optional
 - Line 10 – Date of Birth
 - Signature line
 - Print name
 - Box to check– certify capacity to sign


17



Forms (cont.)


- **Form 8233 - Exemption from Withholding on compensation for Independent (an certain Dependent) Personal Services – last updated June 2011**
 - Purpose: To claim tax treaty withholding exemptions from:
 - Compensation for independent personal services performed in the U.S.
 - Compensation for dependent personal services performed in the U.S.
 - Noncompensatory scholarship or fellowship income and personal services income from the same withholding agent.
 - FILED Annually with the IRS!

18


Forms (cont.)


- **Form 8233**
 - Answer all applicable questions COMPLETELY
 - Specify the tax year
 - Attach the required statement described in line 10 for foreign student, trainee, professor/teacher, or researcher
 - Complete 11-14 in sufficient detail to allow the IRS to determine the tax treaty benefit you are claiming.
 - Claim the proper number of personal exemptions on line 15.
 - Complete required certification on Part 3.

19


Forms (cont.)

- **Employee and Self-Employment**
 - Example: A nonresident alien is primarily present in the United States as a professor, but also is occasionally invited to lecture at another educational institution. These lectures are not connected with his teaching obligations but are in the nature of self-employment.
 - For each year the professor must complete TWO forms 8233 and give one to each withholding agent to claim tax treaty benefits on the separate items of income.
 - What issues do you see with this... are there any?

20


Forms (cont.)

- **Noncompensatory Scholarship**
 - Example: XYZ University awards a scholarship to Judy, a nonresident alien student. The only condition of scholarship is that Judy attends classes and maintains a minimum level of academic performance. The scholarship income is not compensatory because Judy is not required to perform services as an employee as a condition for receiving the scholarship

21

Forms (cont.)

- **Form W-4 - Employee's Withholding Allowance Certificate**
 - Line 2 - Required to enter SSN
 - Line 3 - Check single box
 - Line 5 - Claim 1 withholding allowance
 - Unless from Canada, Mexico, or South Korea; a student from India; or a U.S. national - claim additional allowances
 - Line 6 - NRA above dotted line
 - Line 7 - DO NOT claim you are exempt

Frequently Asked Questions - IRS

- **Responsible for the validity of documentation presented by foreign payee?**
 - To rely on documentation, it must be valid!
 - To be valid - the documentation must meet the requirements of Treasury Reg. 1.1441 and must be completed in accordance with the applicable form instructions
 - To be valid - the withholding agent must not know, or have reason to know, that the information provided on the documentation is unreliable or incorrect.
 - If the documentation is invalid for any reason, the withholding agent must apply the presumption rules set forth in Treasury Reg. Section 1.1441.1.

Are you still awake????

- **Where do you keep your Tax Assessment Documentation?**
 - A. Human Resource Maintains this in the HR File
 - B. We maintain a separate file
 - C. We don't maintain any records of tax assessments
 - D. All the above.
 - E. This doesn't apply to me.

Please chat in your answer

Are you ready for Year-End Processing???

- **Who is your population**
 - Audit your databases
 - Payroll
 - Accounts Payable
 - Student Accounts
 - Determine a schedule auditing your databases
 - Around Payment Schedules
 - Quarterly for Payroll and Accounts Payable
- **Work with the various departments to share information**
 - I-9s
 - Contracts
 - Invoices/Purchase Orders
 - Communication to Various Departments is crucial


Are you ready for Year-End Processing??? (cont.)

Reviewing your Systems and Files

- HR/AP System (example: PeopleSoft, Banner or NCAS)
 - Visa Panel
 - Tax Panel
 - Queries
 - I-9's
 - W-9's or W-8's
- International Students, HR, Accounts Payable, etc.
 - Building relationships with the groups that sponsor your foreign nationals' visas.
 - Building relationships with your department representatives (HR or Payroll).
- International Tax Navigator
 - Where you store all this information and produce your tax documents.

IRS Recommendation for Identifying Foreign National


- Address Field
 - Country – not U.S.A. or Blank
 - State – not a U.S. State or Blank
 - City – Foreign City
 - Zip – not a U.S. pattern – XXXXX-XXXX
- Foreign Employer I.D. Number
 - Usually begins with 99-XXXXXXX
- Foreign ITIN
 - Usually begins with 999 and 4th digit is a "4" or "7"
- Foreign Vendor Numbers
 - Required by accounting system?
 - Do you have a policy for establishing "fake" vendor numbers?



Critical Questions

- **Visa/Immigration Information within systems:**
 - Who updates your data?
 - Training
 - Are you utilizing this panel properly?
 - Have you left this panel blank?
 - Is the information in this panel accurate?
 - How are you tracking data/expirations?
- **I-9 Issues**
 - Accepting a restricted SSN for List C.


28



Processing Suggestions/Reminders

- **Checklist**
 - Documents necessary documentation
 - Provides an audit trail for compliance
 - Easily accessible for annual assessments
 - Organized documentation for USCIS or IRS Audit
- **Foreign National Processing**
 - Initial meeting with foreign national – often times in August
 - Annual processing – December/January timeframe (every year)
 - Change in status – who should the foreign national notify?
 - Change in location of employment – SEVIS update necessary?

29



Common Payment Issues


- Please Keep In Mind: **EVERYTHING is taxable unless the Code specifically exempts the type or variety of income**
- **Accountable Plan**

If the requirements of the accountable plan rules are found in Treasury Regulation 1.62(c), and they require that the payee (1) establish the business purpose and connection of the expenses, (2) substantiate the expenses claimed to the payer within a reasonable period of time and (3) return any amounts to the payer if they are over and above the substantiated business expenses within a reasonable period of time. Amounts which are over and above the substantiated business expenses, or not accounted for within a reasonable period of time, are reportable to IRS on Form 1042-S and subject to withholding of employment taxes (or are reportable on Form 1042-S and subject to section 1411 withholding, as applicable).

 - **Have a bona-fide business purpose:** The IRS may view a disbursement as providing a personal benefit if there is any doubt concerning its business purpose. Even though, in some cases the business purpose may be implied, it must be specifically documented so that a third party would have no question as to its benefit to the institution. Paying or reimbursing for "lavish or extravagant" expenses is unacceptable.
 - **Be properly substantiated:**
 - Receipts
 - Per Diem
 - **Be accounted for on a timely basis:**
 - Reasonable period of time


Source: <http://www.irs.gov/individuals/international/Taxpayers/NonresidentAliens-and-the-Accountable-Plan-Rules>

30


Common Payment Issues (cont.)


- **Accountable Plan Reimbursements:**
 - Employee attends a conference
 - Independent Contractor
 - Honorarium expenses (not allowed by State Agencies).
- **Nonaccountable Plan Reimbursements:**
 - Student attends conference to present research paper
 - Volunteering without work authorization

31


Common Payment Issues (cont.)


- **Artist and Athletes**
 - Authorization to perform activity?
 - Central Withholding Agreement (CWA)
 - Provides the appropriate tax rate, if any
 - Issues with obtaining Immigration documentation
 - Require as part of your contract
 - Rise in the use of Business Profit Articles
 - Please use caution!!!!
- **REMINDER:**
 - Even if an individual has violated his immigration status and has performed services for you not authorized, you must pay the compensation and tax and report the payment accordingly
 - You cannot cure an immigration violation by refusing to pay for services

32


Common Payment Issues (cont.)

- **Software**
 - Renewable yearly - taxable
 - Customized - taxable
 - One-time Purchase – it depends
- **Cloud Sourcing**
 - Where are the servers located?
 - Unable to determine – better to tax or exempt under treaty
- **Subscriptions (Access to Databases)**
 - Where is the server located?
 - Where is the property used?

33



Common Payment Issues (cont.)


- Scholarships – Publication 970**
 - Qualified Scholarships are exempt from taxation under section 117, but requires
 - Recipient is a "Candidate for a Degree"
 - Awarded to study at an "Educational Organization"

Table 1-1. Tax Treatment of Scholarship and Fellowship Payments
Recipients should consult with a tax advisor for complete details.

If you are the recipient of the payment	Are you an...		Will your payment be...	
	A degree candidate	Not a degree candidate	Tax free ¹	taxable
Tuition	X	X	X ²	X
Books	X	X	X ²	X
Supplies	X	X	X ²	X
Equipment	X	X	X ²	X
Room	X	X		X
Board	X	X		X
Travel	X	X		X

1. This section applies to awards of cash and other property.
 2. This section applies to awards of cash and other property for the recipient's education.
 3. Recipients of all awards should consult with a tax advisor.


34



Common Payment Issues (cont.)

- Scholarship Disbursements**
 - Statutory Rate (F, J, M, Q) – 14%
 - SSNs
 - Application Process
 - Necessary documentation
 - Qualified vs. Non-Qualified
 - Sourcing
- Funding**
 - Assistantship not listed on Immigration Documents
 - Work Authorization
- Vendor/Contractor Payments**
 - Review of each invoice for taxation
 - Method of payment?
 - Vendor entry in accounting system

35



BEST PRACTICE!!!

Best practices in making payment to nonresident aliens (NRAs)

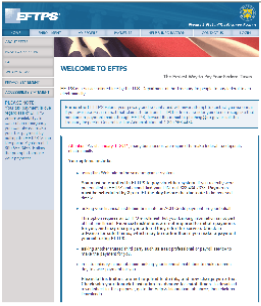
- Implement policies and procedures for meeting IRS due diligence.
 - Recommend posting them to your website
- Keep up-to-date on rules and forms procedures – they have changed drastically this year!

Immigration risk for your institution

- Unauthorized workers performing services
 - Non-sponsored employees performing services for your institution
 - Foreign nationals not authorized to perform independent services
 - Have you established a process to ensure your departments know who they can and can't contract with?

36

Tax Deposits – Easiest Area for Penalties and Interest



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

Tax Reporting

U.S. Citizens or Resident Aliens	Nonresident Aliens
<ul style="list-style-type: none"> Tax on Worldwide Income <ul style="list-style-type: none"> Entities org. under U.S. laws W-4/W-2/NC-4 <ul style="list-style-type: none"> Standard Wage Withholding W-9/1099 <ul style="list-style-type: none"> 28% backup withholding \$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"> Tax on U.S. Source Income <ul style="list-style-type: none"> Not org. under U.S. laws W-4/W-2/NC-4/NRA <ul style="list-style-type: none"> NRA Tax Rate W-8s/8233/1042-S <ul style="list-style-type: none"> 30% withholding State Taxes (NC 4% > \$1500) No minimum dollar threshold for payments Treaty benefits or ECI to reduce U.S. tax/withholding, if qualify Filing deadlines <ul style="list-style-type: none"> Payees: 3/15 (W-2: 1/31) IRS: 3/15-4/14 NC DOR: 2/28 Electronic Filing



Summary

- Reviewed facts necessary to process payments
- Awareness of changes to forms
- How to identify your population to create foreign national files
- Common Payment Issues
- Be prepared for an IRS audit – where is your audit trail?????

Questions?

Contact Information:
Jennifer Pacheco
NC Office of State Controller
Foreign Nationals
Tax Compliance Program
919-707-0764
jennifer.pacheco@osc.nc.gov

- For additional training opportunities please visit:
- http://www.osc.nc.gov/Foreign_Nationals/training.html



THANK YOU!

40
