


## FOREIGN NATIONALS TAX COMPLIANCE TRAINING

### The 5 "W's" of Foreign Nationals Tax Compliance How to Implement These 5 W's


**April 29, 2014**



### 2014 Training Curriculum


This training is an Office of State Controller initiative and is part of the Foreign Nationals Tax Compliance curriculum for the 2014 calendar year. We are committed to the success of the Foreign Nationals Tax Compliance Program and will provide technical assistance to all State Agencies, Universities, Community Colleges, LEAs and Charter Schools.

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.





NC Office of State Controller



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### Training Agenda – What are the 5 W's + 1H





### WHY????


### You Know WHY We Are Here.... Does Your Departments Know WHY???

- **Per Internal Revenue Code 1441 to 1443** – Governs withholding on payments of U.S. source income to foreign persons and provides for the 30% tax
- **TAX Liability:** Per IRC Section 1461 - The withholding agent will be liable for a tax amount resulting from failing to withhold or deposit amounts subject to NRA withholding. Both the withholding agent and the foreign recipient may be held liable for such tax, applicable interest and any penalties resulting from a withholding failure.
- **Per IRS Publication 515:** "This publication is for withholding agents who pay income to foreign persons, including nonresident aliens, foreign corporations, foreign partnerships, foreign trusts, foreign estates, foreign governments, and international organizations."  
Specifically, it describes the:
  - persons responsible for withholding (withholding agents)
  - the types of income subject to withholding, and
  - the information return and tax return filing obligations of withholding agents

**You Know WHY We Are Here....  
Does Your Departments Know WHY???** (cont.) 

- Withholding Agent
  - A U.S. or foreign person that has control, receipt, custody, disposal, or payment of any item of income of a foreign person that is subject to withholding
  - Liable for taxes owed
- Foreign National
  - An individual that owes allegiance to or who is under the protection of a country other than the United States
    - > Non-Resident Alien
    - > Resident Alien

7

**WHY Do I Need to Process Foreign Nationals Differently???** 


- Foreign nationals have a special set of work restrictions and tax guidelines they must follow.
- Ensure appropriate documents are received
- Provide necessary communication to foreign nationals
- COMPLIANCE ISSUES:
  - Each entity is at risk of very large penalties and fines
  - Potentially jeopardizes the foreign national's visa status.

8

**WHO???** 




9

**WHO is an Non-Resident Alien?** 


<u>Immigration</u>	<u>Taxation</u>
> United States Citizens	> United States Citizens
> Lawful Permanent Resident	> Lawful Permanent Resident
> Foreign National	> Non-resident Alien for Tax Purposes <b>OR</b> > Resident Alien For Tax Purposes

10

**WHO is an Non-Resident Alien?** (cont.) 

- Temporary (nonimmigrant) status
  - Limited by:
    - > Time – duration of authorized period of stay
    - > Scope – allowable activities
    - > Location – employer as well as physical presence
  - Must have nonimmigrant intent
  - Generally denoted by alphabetical notation
- Permanent (immigrant) status
  - Allows holder to remain in U.S. indefinitely
  - Permanent Resident can live and work wherever, and for whomever s/he chooses – no limitations based on time, scope or location
  - “Green card” is another way to indicate someone has permanent resident status
  - Treated just like a US citizen for taxation purposes

11

**WHO is an Non-Resident Alien?** (cont.) 

- Non-resident Alien for Tax Purposes
  - Individuals who are not U.S. citizens, permanent residents, or resident aliens for tax purposes are considered to be **non-resident aliens for tax purposes**.
  - To determine if a foreign national is in resident alien tax status or non-resident alien tax status we must calculate the IRS's **Substantial Presence Test (SPT)**
  - Non-resident aliens have a **tax system different** from U.S. residents. Their income is subject to different withholding rules and reporting.
  - Non-resident Aliens must first be **eligible for employment** as determined by U.S. Citizenship and Immigration Services (USCIS).
- Resident Alien for Tax Purposes
  - Means something different to IRS than USCIS
  - Passes the Substantial Presence Test (SPT)

12



### Majority of Visa Types you will see:

**Teachers, Researchers and Temporary Employees**  
H-1B, TN, O-1, as well as all other visa categories  
Foreign Nationals with a valid Employment Authorization Card (EAD) may receive wages  
Employment is permitted only if the card has not expired  
*Sponsored by you entity*

**Students and Researchers**  
F-1, J-1, and M-1  
F-1 Optional Practical Training (OPT): must have EAD  
*Sponsored by you entity*


**Trainees and Camp Counselors**  
F-1 or J-1  
Honoraria  
B-1/B-2, VWB, VWT, ESTA  
*Only for Higher Education*

**Athlete, Artist, and Entertainers**  
P-1, P-2, P-3  
*Sponsored by you entity or listed on Itinerary*

**Cultural Exchange Program**  
Q-1, Q-2

Please refer to the Visa and Payment Chart for more detailed information.

13




### Who Am I Paying???

Resident Alien (RA) or Non-resident Alien (NRA)

- **Determines:**
  - Income subject to tax – RA (Worldwide) or NRA (US Only)
  - Whether certain treaty exemption apply
  - Withholding certificate for treaty benefits and other tax forms
    - 8233, W-8BEN, W-8BEN-E
    - Must have a U.S TIN
    - W-4
    - W-9

14



### Who Am I Paying???

(cont.)

- Who is the beneficial owner of the income
  - Foreign Individual
  - Foreign "Company"
  - Foreign Government
  - Foreign Exempt Organization
- Payments to Foreign Performers
  - Agent for the Foreign National
- Source
  - U.S. Source
  - Foreign Source
- Who is eligible to perform services?
- Substantial Presence Test (SPT)


15



### WHAT???




16



### HELP!!! WHAT If I don't Who I'm Paying?

- How to identify my population
- What to do once I identify my population
- What are my tools to process my population


17



### Tips for identifying a Foreign National


- If your entity shares information you can learn about someone's immigration status from:
  - I-9's
  - Social Security Cards (Is there a notation on the card?)
  - Human Resource databases
- For taxation purposes – you are allowed to ask for immigration information and documentation
- Audit to determine you population

18




### Tips for identifying a Foreign National (cont.)

- Publication 515 – **Presumption Rules**. “if you cannot reliably associate a payment with valid documentation you must apply certain presumption rules or you may be liable for tax, interest, and penalties.”
- It is better to tax and have those taxes refunded by the IRS to the individual, than to not tax at all and face penalties and fines.




19



### Tips for identifying a Foreign National (cont.)

- A newly-arrived payee already has an SSN but has represented that they have no prior presence in the U.S.
- Country of Visa issuance or foreign residence is different than county of tax residency claimed by payee.
- Situations where a business entity is payee, but the true beneficial owner of the income is an individual.
- A payee asking you to make payment to a charity or foundation instead of them.
- U.S. Port of entry stamps or visas in an individual's passport that are not mentioned in the individual provides to you.


20



### WHAT Type of Payments

- The type of payment made to an vendor, employee, student falls into four primary categories:
  - **Dependent personal services:** Wages, Service related scholarship/fellowship/assistantship payments, travel reimbursements
  - **Independent personal services:** Consulting fees, guest speaker, honoraria
  - **Scholarship/Fellowships:** Qualified/Nonqualified
  - **Other Income Types:** Prizes and awards, royalties, etc.
- **Gift Cards** = Cash
- **Stipends** = One of the above

21




### WHAT is being purchased????

- Goods from a foreign entity
  - No withholding or reporting required
- Services performed outside the U.S.
  - No withholding or reporting required, in most cases
- Services performed in the U.S.
  - Taxable at federal 30%, unless treaty exist
  - Potentially taxable at NC state 4%, unless treaty exist
  - Independent Personal Services
- Royalties used in the U.S. (Copyrights and Software)
  - Taxable at federal 30%, unless treaty exist

**Potential exceptions may exist.**

22




### WHAT is the Source of the Income

A determination is made as to the source of income in the following manner:

- Compensation paid to employees and independent contractors
  - sourced = country where services are performed.
- Non-compensation Payments
  - scholarships/fellowships
  - grants, prizes and awards
  - source = residence of the payor regardless of who actually disburses the funds

23



### WHAT Payment Subject to Income Tax Withholding?

- **Resident Alien** – same rates as 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 (\$1,500 threshold)
  - Tax Treaties

24

**HOW????**

25

**HOW to Ensure Successful Processing**

- Having Written Policies and Procedures Will...
  - Make your job easier
  - Reduce frustration for everyone
  - Help departments and payees understand what to do and why
  - Will aid in more efficient processing of payments
  - Increase institutional compliance
  - Show the IRS you take compliance seriously
- High-level Policies:
  - Define institution's commitment to complying with IRS, immigration, federal, state, local and other regulations
- Internal Operational Policies:
  - Day-to-day implementation policies; based on what can and cannot be done within framework of high-level policies

26

**HOW to Begin Documentation**

Data Gathering Form should be completed by each foreign national and presented with originals of the specified immigration documentation (copies should be made).

- Used to determine:
  - Eligibility for payments dependent on visa type
    - > Determine tax status is Non-resident Alien or Resident Alien (Substantial Presence Test)
  - OSC Checklist

27

**HOW to Process**

WINDSTAR: A valuable software that stores all your foreign national information and produces your tax documents.

- Functions of Windstar:
  - Runs the Substantial Presence Test
  - This software can produce:
    - > W-4
    - > W-8BEN
    - > W-8BEN-E (coming soon)
    - > 8233
    - > W-9
  - Produces 1042-S and 1042 forms.
  - Assists with electronic 1042 submission file.
  - Runs useful reports.

28


**HOW To Report**

Nonresident Alien	Resident Alien
<ul style="list-style-type: none"> <li>• Payments are reported to the federal government in the following manner:                             <ul style="list-style-type: none"> <li>- Forms Issued                                     <ul style="list-style-type: none"> <li>&gt; W-2 – Taxable Employment Income</li> <li>&gt; 1042-S   <ol style="list-style-type: none"> <li>1. Any treaty-exempt income</li> <li>2. All other U.S.-Source Taxable Income and Taxes Withheld – Form 1042-S</li> </ol> </li> </ul> </li> <li><b>NO Form 1099</b></li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Payments reported in the same manner as U.S. Citizens.                             <ul style="list-style-type: none"> <li>- Forms Issued                                     <ul style="list-style-type: none"> <li>&gt; W-2 – Taxable Employment Income</li> <li>&gt; <b>1099</b> <ol style="list-style-type: none"> <li>1. Non-employee Compensation</li> <li>2. Other Income</li> </ol> </li> <li>&gt; 1042-S   <ul style="list-style-type: none"> <li>- Any treaty-exempt income</li> </ul> </li> </ul> </li> </ul> </li> </ul>

29

**WHEN????**


30



### WHEN Taxes on Paychecks May Be Avoided

- Compensation paid to NRA employees is subject to a grossed up withholding
- Restrictions on W-4
- Students:
  - International **students** on F-1, J-1, M-1 or Q-1 visas are exempt from paying Social Security and Medicare taxes – (5 calendar years; see IRS Publication 515)
  - After 5 calendar years they will continue to be **exempt** as long as they are enrolled in classes at least ½-time AND work less than 30 hours per week – (“The Student Rule”)
- Some of a foreign national's wages may be exempt from Federal and State income taxes because of a tax treaty between their country and the United States.

31




### WHEN Taxes on Paychecks May Be Avoided (cont.)


Considerations When Granting Treaty Benefits

- U.S. tax status: NRA or RA
- **Provide Social Security Number or ITIN**
- **Country of tax residency**
- Primary purpose of visit as evidenced by
  - DS-2019 for J Exchange Visitors
  - I-797 approval notices for H-1B, O-1, Q
  - I-20 for F and M visitors
- Status of the organization (educational, research, medical, etc.)
- Type of Income Paid
- Conducting research, teaching, training, other paid activities (honorarium activity)

32



### WHEN Tax Deposits MUST be Made:



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


33



## Most Common Questions

# ???

34




### Most Frequent Questions

Accountable Plan or NOT

- “Accountable Plan” Rules **ONLY** apply when there is a compensatory relationship
- “Accountable Plan” Rules **DO NOT** apply if there isn't compensatory relationship

35



### Most Frequent Questions (cont.)

Honorarium vs. Contracted Services

- 9/5/6 Rule:
  - Visitor is limited to 9 days presence at an institutions to be eligible for honoraria payment
  - Visitor cannot have visited more than 5 institutions in the past 6 months
- Visa Type:
  - Visitor needs to enter the U.S. on a B visa (preferably B-1, not B-2), or as VW national (Visa Waiver program)
  - If the visitor is on any other type of visa, you must determine if permitted to pay an honoraria
- Services Required = Compensation ≠ Honorariums

36

**Most Frequent Questions (cont.)**

Honorarium Documentation (potential):  
To pay honorarium, you must have copies of:

- Passport identification page with picture, expiration date
- Nonimmigrant visa (B-1/B-2) or I-94 card (VW)
- I-94 card issued by CIS/CBP (small white card/electronic)
- Social Security card, ITIN card, or Unknown Social Security affidavit
- Section 431 compliance statement
- W-8BEN
- Permanent Residence Address (outside of U.S.)
- Dates of visit to agency (9-5-6 Rule)
- Potential Treaty Benefits

**Is your entity permitted to pay honorariums?**

37

**Most Frequent Questions (cont.)**

- Form 8233 with Certifying Statement from NRA
  - TIN Required
    - Can attach copy of SSN application receipt
  - Must submit to IRS within 5 days of accepting (signing)
  - IRS has 10 days to reject treaty
- Form W-8 BEN
  - Purpose – what country does the individual have a closer connection with?
  - Treaty Benefits
    - TIN REQUIRED!!!
  - Do we submit this to the IRS?

38

**Most Frequent Questions (cont.)**

- Special Handling is required for payments to F-1 and J-1's from other universities/community.
- Required to ensure F-1 or J-1 is still in status.

39

**WHERE????**



40

**HOW to Be Successful**

- Ensure you are kept in the Loop!!!!
- Market yourself and your services
- WHERE is Your Agency in Preparation for IRS or USCIS Audit!!!!
  - Scope:
    - Written Policies and Procedures
    - Paperwork processing flow
    - Training for staff
    - Self review/audit
  - Process Flow
    - Who is the Primary Contact(s), aka Non-resident Alien Tax Specialist for each area
    - How is your filing/documentation System
    - Determination of Withholding and Reporting

**Are you READY for an IRS review?**

41

**WHERE can I find the following forms**

- W-8 ECI
  - Effectively Connected Income
  - Business Location within the U.S.
  - Must have a U.S. TIN
- W-8 BEN (Individual)
  - New Form released February 2014
  - More Concise
- W-8BEN-E (Entity)
  - Implement by the end August 2014 (6 months after release)
  - 8 pages
  - No directions

**IRS - <http://www.irs.gov/uac/Form-W-8,-Certificate-of-Foreign-Status>**

42

**The Daily Questions**

- Who?
- What?
- When?
- Why?
- Where?
- How?



43

**Questions?**



44

**FNTICC**  
FOREIGN NATIONAL TAXATION & IMMIGRATION COMPLIANCE CONFERENCE

**SAVE THE DATE**  
Wednesday, October 8 - Thursday, October 9, 2014

**NC STATE UNIVERSITY**



45

**Contact Information**

- Any questions that are not handled within the presentation will be responded to via email.
- Follow-up questions can be submitted to Jennifer Pacheco, with the NC Office of the State Controller, at [jennifer.pacheco@osc.nc.gov](mailto:jennifer.pacheco@osc.nc.gov) or 919-707-0764.
- For additional training opportunities please visit:
  - [http://www.osc.nc.gov/Foreign\\_Nationals/training.html](http://www.osc.nc.gov/Foreign_Nationals/training.html)

46

**THANK YOU!**

47