



FOREIGN NATIONAL TAX COMPLIANCE TRAINING

“Best Practices” and “Policies and Procedures Update” for State Agencies, Universities and Community Colleges

OCTOBER 15, 2009



Panelist

- **NC State University Human Resources and Payroll Division**
 - Michelle Anderson, Foreign National Tax Specialist
- **NC Community College System Business and Finance Division**
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- **Windstar Technologies, Incorporated**
 - Paula Singer, Co-Founder and Chair of Windstar Technologies, Inc.
- **NC Office of the State Controller**
 - David Reavis, Director E-Commerce Initiatives
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2009 Training Curriculum

- This training is an Office of State Controller Initiative, in collaboration with Windstar Technologies, NC State University and the Community College Systems office. This training is part of the Foreign National Tax Compliance curriculum that the Office of State Controller has planned for the 2009 calendar year. The Office of State Controller is committed to the success of the Foreign National Program and will provide technical assistance to all State Agencies, Universities, and Community Colleges.



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. 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 National Program within their State Agency, University or Community College. 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.



How to ask questions

Asking Questions:

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To ask questions select "Q&A". Then type in the box.

The screenshot shows a WebEx Event Manager window titled "WebEx Event Manager - Test". The main content area displays a presentation slide with the following text: "Nonresident Alien Tax Training", "Rules of the Road for NRA Taxation", and "Presented by: Paula Singer, Esq.". To the right of the slide are five small portrait photos of participants. On the right side of the window, there is a "Participants" panel with a table listing "Panelists: 1" (Paul Carpinella (Host)) and "Attendees: Paul Carpinella". At the bottom of the window, there is a control bar with buttons for "Raise Hand", "Request", "Mute", "Chat", and "Q&A". The "Q&A" button is highlighted with a white box, and a black arrow points from the text box above to it. The Windows taskbar at the bottom shows the Start button, several application icons, and the system tray with the time "9:38 AM".



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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Forms, Filing, and Immigration Risks

- 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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Forms, Filing, and Immigration Risks

- Withholding certificates
 - W-4 under new NRA Rules
 - 8233 for treaty benefits for NRA compensation (required annually)
 - W-8BEN for treaty benefits for all other payment types
 - W-9 for treaty benefits for Resident Aliens (RAs)

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Forms, Filing, and Immigration Risks

- Year-end reporting
 - 1042-S information return for NRAs
 - 1042 tax return required if any Forms 1042-S are issued (even if all are for treaty exemption and have no tax withholding)

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Forms, Filing, and Immigration Risks

- Nonresident Aliens
 - W-2 reporting for wages subject to wage withholding and FICA wages and taxes
 - 1042-S for treaty-exempt income (including treaty-exempt wages)
 - 1042-S reporting for all other income payments (**not** 1099!)
 - Form 1040NR or 1040NR-EZ Tax Return

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Forms, Filing, and Immigration Risks

- Immigration risk for your Agency
 - Unauthorized workers performing services
 - Non-sponsored employees performing services for your agency
 - Foreign nationals not authorized to perform independent services

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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.



Policy (cont.)

- 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.



Procedures

6 Steps for Paying or Compensating Aliens:

- Step 1** – The Payee-Payment Eligibility and Tax Residency Status
- Step 2** – The Type of Payment
- Step 3** – The “Source” of the Income
- Step 4** – Payment Subject to Income Tax Withholding?
- Step 5** – Is the Payment Subject to FICA?
- Step 6** – Determine if Payment is Reportable and How?

Step 1 – The Payee-Payment Eligibility and Tax Residency Status



- A Foreign National Information System Data Gathering Form should be completed by each foreign national and presented with copies of the specified immigration documentation.
 - Used to determine:
 - Eligibility for payments to be made based on the type of visa issued (Refer to page 28 of Policies and Procedures Manual)
 - Determine if the Payee's tax status in Nonresident Alien or Resident Alien (Substantial Presence Test)



What Tax Status Determines

- The Starting Point: Tax Residency Status-
 - Resident Alien (RA) or Nonresident Alien (NRA)
 - Determines:
 - Income subject to tax-Resident Alien (Worldwide) or NRA (US Only)
 - Form W-4 and FIT rules
 - Internal Revenue Code tax exemptions
 - » NRA FICA Exceptions
 - Whether certain treaty exemption apply
 - Withholding certificate for treaty benefits

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The Substantial Presence Test (SPT)

- A 183-day formula based on:
 - Current status and date of entry
 - Also expected departure date
 - 3-calendar year history of U.S. visits
 - Longer history if any visits in most recent 3 years are/were in F, J, M, or Q Status

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Step 2 – The Type of Payment

- The type of payment made to the alien 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.



Various Payment Types

- Payment types
 - Payroll (employee wages)
 - Non-service fellowship grants (including travel grants)
 - Accounts payable (non-employee compensation)

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Step 3 – The Source of the Income

- **Resident Alien**-Income is generally subject to tax in the same manner as a U.S. Citizen.
- **Nonresident Alien**-is usually subject to U.S. income tax only on U.S. source income.



Step 3 – The Source of the Income(cont.)

Nonresident Alien

- 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 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.



Step 4 – Is the Payment Subject to Income Tax Withholding?

- **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
- **Nonresident Alien**-all U.S. sourced income is taxable with a few exceptions.
 - Tax Rate 14%-30%
 - NRAs wages are also subject to the American Recovery and Reinvestment Act.
 - Tax Treaties



Treaty Benefit Eligibility and Payments to NRAs

- The U.S. has treaties with over 60 countries around the world affecting payments to foreign nationals
- Treaties offer tax exemptions for foreign nationals who were or are tax residents (not citizens) of a treaty country and meet specific criteria
- Many foreign nationals understand and expect these benefits
- The IRS requires organizations to comply with its rules and procedures when granting benefits

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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-129 petition and letters 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)

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Step 5 – Payment Subject to FICA?

Nonresident Alien

- The only aliens exempt from FICA are the following Nonresident Alien visa holders:
 - F-1
 - J-1
 - M-1
 - Q-1
- The above visa holders are subject to FICA taxes for the entire year they become resident aliens.



Payroll - NRA Wage Withholding Rules

- See IRS Publication 15T
- Requires employers to augment wages with an amount that reflects the standard deduction built into the wage withholding tables
 - Exception for residents from India who are business apprentices or students.
- New withholding tables were developed due to changes to the tax law made by the American Recovery and Reinvestment Act of 2009, the amount to add to a nonresident alien employee's wages for calculating income tax withholding only has been increased.

<u>Payroll Period</u>	<u>Add Additional</u>
Biweekly	\$276
Monthly	\$598
Annually	\$7,180



Step 6 – Determining if a Payment is Reportable and How

Resident Alien

- Payments are reported in the same manner as U.S. Citizens.
 - Forms Issued
 - Taxable Employment Income-Form W-2
 - Statement for Non-employee Compensation and Back-up Withholding, if any – Form 1099
 - Other Reportable Taxable Income – Form 1099
 - Any treaty-exempt income, including but not limited to wages – Form 1042-S



Step 6 – Determining if a Payment is Reportable and How (cont.)

Nonresident Alien

- Payments are reported to the federal government in the following manner:
 - Forms Issued
 - Taxable Employment Income – Form W-2
 - Statement for Non-employee Compensation and Taxes Withheld – Form 1042-S
 - Any treaty-exempt income, including but not limited to wages – Form 1042-S
 - All other U.S.-Source Taxable Income and Taxes Withheld – Form 1042-S

Please note Form 1099 **cannot** be issued to nonresident aliens!



Withholding requirements for NRAs

- General Rule: 30% withholding Tax
- Exceptions
 - 14% on taxable grants of F, J, M and Q candidates for degree and F, J, M, and Q non-degree candidates if granted by a qualifying entity (Section 1441 (b)(2))
 - Wages subject to wage withholding

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Doing More with Less.....

Resources

- Foreign National Tax Compliance Website
 - http://www.osc.nc.gov/Foreign_Nationals/
 - Information: Updated Policies and Procedures-August 2009
- Windstar User Website
- Windstar List Service
- Tax Treaty Benefits for Foreign Nationals Performing U.S. Services (purchase from Windstar)
- NC State University Website
 - <http://www7.acs.ncsu.edu/hr/payroll/fntax/>



Doing More with Less...(cont.)

Resources

- Office of State Controller
 - Jennifer Trivette - jennifer.trivette@osc.nc.gov
- North Carolina State University
 - Michelle Anderson – michelle_anderson@ncsu.edu
- Foreign National Tax Compliance Training Curriculum
 - http://www.osc.nc.gov/Foreign_Nationals/training.html
- NCSU HR Academy Classes
 - <http://www7.acs.ncsu.edu/hr/tod/hracademy.asp>



Where to Find More Information

- Easy-to-read tax treaties and *View from the Crow's Nest* archives at www.windstar.com
- www.irs.gov click on Individuals, click on International Taxpayers
- www.nafsa.org for information on government procedures affecting foreign students and exchange visitors

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Where to Find More Information

- IRS Publications (www.irs.gov)
 - 15T, Employer's Tax Guide
 - (http://www.irs.gov/publications/p15t/ar02.html#en_US_publink1000145960)
 - 515, Withholding on Nonresident Aliens and Foreign Entitles
 - 519, US Tax Guide for Aliens
 - Internet Search Engine (Google)



What is an IAT?

International ACH Transactions



What are the IAT Rules?

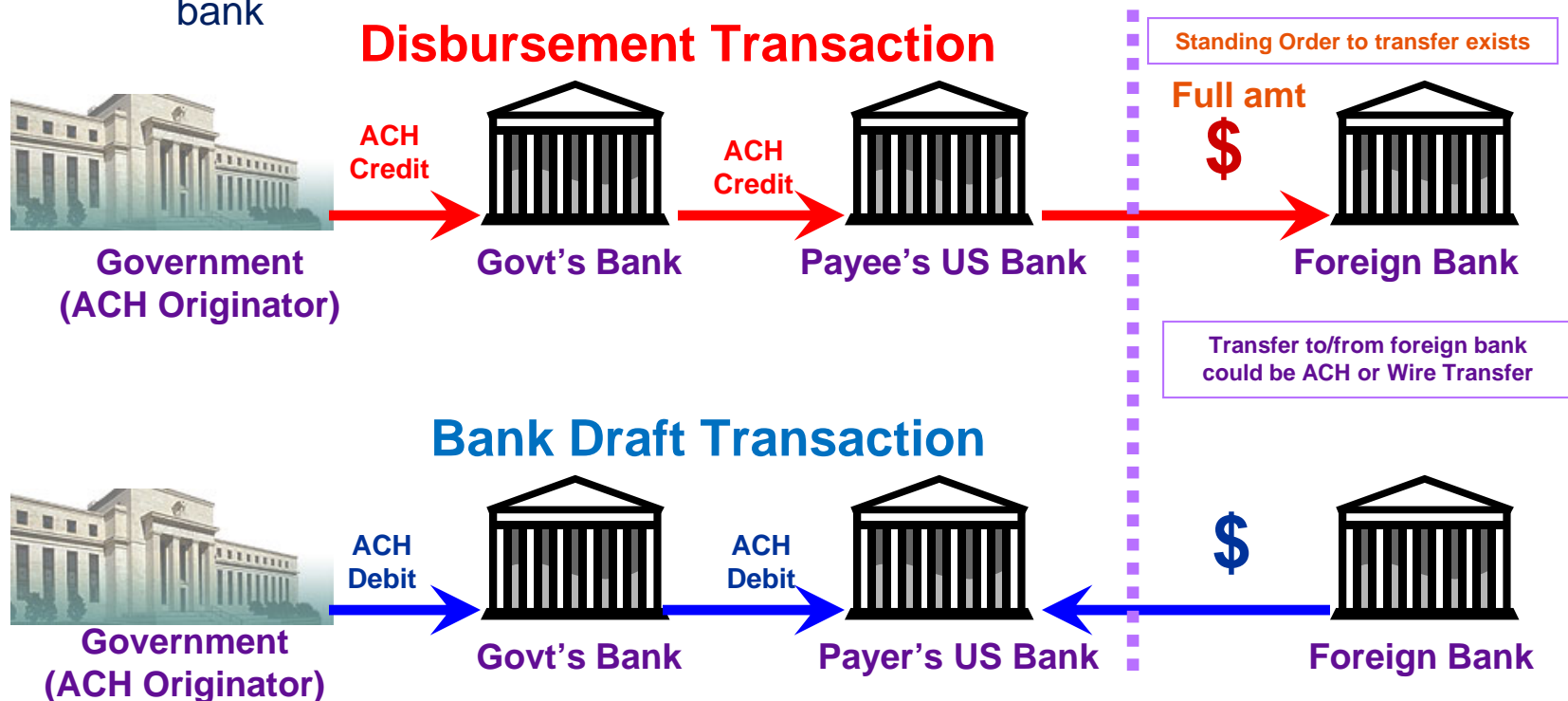
- A subset of the National Automated Clearing House Association (NACHA) Operating Rules that became effective September 18, 2009
- Rules are a result of NACHA amending the Operating Rules to address requirements of Office of Foreign Assets Control (OFAC) – Part of US Treasury Department
- OFAC enforces economic and trade sanctions against targeted foreign countries, terrorists, international narcotics traffickers, those engaged in proliferation of weapons of mass destruction, etc.
- OFAC maintains a “do not do business with” list (SDN List)
- Rules designed to involve companies and governments in the process by assisting banks in performing their screening process for ACH transactions
- Potential fines violation of US Law (\$10,000 - \$10,000,000)
- If an ACH payment meets definition of an IAT, government must create a special ACH file before sending to the originating bank, otherwise must pay by paper check



What is an IAT?

• An electronic payment originated through the Automated Clearing House Association that is either part of a set of transactions where:

- The funds associated with the payment are remitted to an off-shore bank, or
- The source of the funds supporting the payment are from an off-shore bank





How to Comply With IAT Rules

- **Government is hindered in that it does not have sufficient knowledge to know if an ACH payment meets the definition of an IAT**
- **IAT Rules define what an IAT is, but does not specify compliance actions – other than to label such transactions with a special entry class code (IAT)**
- **OFAC law provides “hold harmless” protection if compliance actions are taken “in good faith.”**
- **Develop policies and procedures that support your “good faith efforts,” incorporating “due diligence” actions**
 - Current ACH Enrollees
 - Future ACH Enrollees
- **How to pay a payee once identified as an IAT payee? – Two options**
 - Discontinue paying by ACH, and pay by check instead
 - Make arrangements to generate ACH file in the special IAT format
- **Policy could recognize potential higher risk for corporate payees (e.g., vendors) than for consumer payees (e.g., vendors)**
 - Employees (e.g., payroll) - there should be “definitive evidence”
 - Vendors - there may be “established conditions”



IAT Rules Resources

Office of Foreign Assets Control

<http://www.ustreas.gov/offices/enforcement/ofac/>

Federal Reserve Bank

http://www.frbservices.org/eventseducation/education/fedach_iat_resource_center.html

National Automated Clearing House Association

http://www.nacha.org/IAT_Industry_Information/

North Carolina Office of the State Controller

http://www.osc.nc.gov/SECP/SECP_IAT_Rules.html

Questions regarding IAT RULES may be submitted to:

David C. Reavis, Director of E-Commerce Initiatives

North Carolina Office of the State Controller

david.reavis@osc.nc.gov

Disclaimer:

You are advised to consult your counsel when implementing IAT rules and OFAC due diligence requirements for your government.

Summary



- Determine the foreign national's U.S. tax status –
Substantial Presence Test
- Perform due diligence with NRA
- Apply applicable treaty benefits
- Complete and file all required IRS forms

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Summary (cont.)

Nonresident Alien Tax Compliance

- Withhold on and report income correctly to avoid unnecessary assessments, fines and penalties
- Provide tax benefits to students, professors, researchers, medical residents, trainees, interns, and independent contractors
- Treaty benefits should only be provided to foreign national's who have either an ITIN or Social Security number
- Be fair but when in doubt be conservative. Better to tax and let them request a refund than not to tax at all and be fined.
- Be prepared for an IRS audit-where is your audit trail?????

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Summary (cont.)

Documentation Practices

- In making payments such as wages, non-service fellowship grants, honoraria, and other independent contractor fees, pensions, royalties, and miscellaneous payment, you need to know:
 - US Citizen, Green-card holder, or other
 - Character of the Income paid
 - U.S. tax residency status of income recipient
 - Source of the payment under U.S. tax rules
 - Conditions allowing exemptions from tax
 - Applicable withholding rates

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Summary (cont.)

International ACH Transactions Rules

- Develop policies and procedures that support your “good faith efforts,” incorporating “due diligence” actions for both current and future payees.
 - Notify all current payees of IAT Rules.
 - Modify “ACH Authorization / Enrollment forms” to allow payee / payer to affirm if their payments are subject to IAT Rules.
 - Include IAT Rules advisement in vendor procurement process (e.g., RFPs).

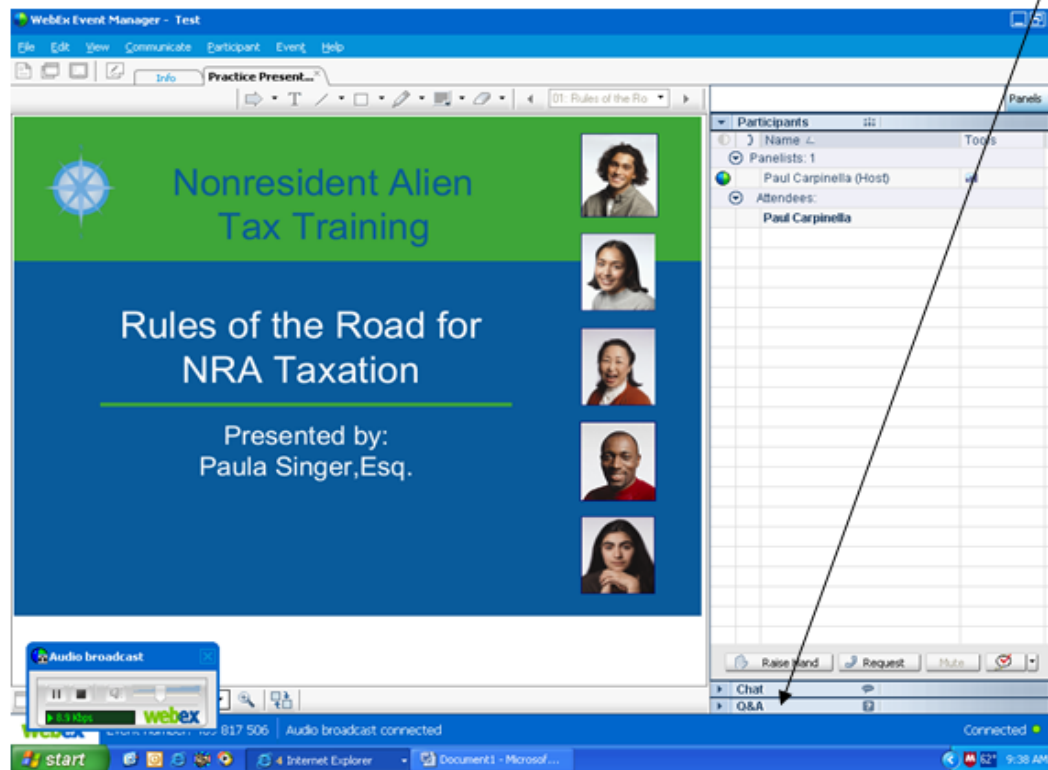


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THANK YOU!