

Guide for Withholding on Payments to Foreign National Vendors

Prepared by Jan Wiersma – February 2010

Payments of any kind to foreign national individuals or entities are treated differently for tax purposes than payments to US individuals or entities. The purpose of this document is to highlight those differences, when withholding of Federal Income Tax (FIT) is required, and the rate of FIT that needs to be withheld from the payment, if applicable.

The IRS determination of a foreign national individual or entity is based on the amount of time present in the US. This is separate from determination by any other governmental agency. Assistance in determining whether the individual or entity is to be treated as a foreign national for tax purposes is available from the Shared Immigration Service (contact information below).

Purchase of Goods:

Purchase of goods from a foreign national individual or entity is not taxable. Therefore, we don't have to do any withholding.

Services Performed OUTSIDE the US

Services that were performed OUTSIDE the US are not taxable. Therefore, we don't have to do any withholding.

Services Performed in the US

If the payment is for services performed by a foreign national while in the US, we need to withhold 30% income tax unless the services are paid through payroll, in which case the withholding is done using the graduated tax tables. This includes payments for honorariums paid to foreign artists, entertainers, speakers, etc.

Tax Treaties might apply to some of these payments. If a tax treaty is available, the foreign national MUST complete a tax treaty form and a form to apply for a tax payer ID number if they don't already have one. This paperwork must be completed before the payment is issued. Items needed to attach to the forms: copies of foreign national's passport, I-94 card, and Social Security card (if available).

Fellowships

Payments to a foreign national fellowship recipient (work performed is for the benefit of the individual only with no benefit to the university) require withhold at a rate of 14% for income tax unless there is a tax treaty that exempts it.

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passport, I-94 card, any documents issued by the US Citizenship and Immigration Service, and Social Security card (if available).

Scholarships

Scholarships paid to a foreign national are only taxable if the amount exceeds the actual cost of tuition and fees, the estimated cost of books (per Financial Aid). If the scholarship exceeds the cost of tuition, fees, and books the overage balance is taxable at 14% unless the foreign national is from a country that has a tax treaty for scholarships. This is monitored centrally by the Shared Immigration Service Office. Campuses are emailed applicable amounts and are notified to collect any applicable taxes through Student Receivables.

Special Reporting to IRS

Any time we collect income tax from a foreign national that is not withheld through payroll, the Shared Immigration Center submits the tax to the State Auditor's Office on a separate voucher which designates the tax as 1042s income rather than W-2 income. The tax has to be either withheld from the payment or paid by the individual. If neither is done, it becomes the responsibility of the campus which must pay the tax on behalf of the individual using the Gross-up method.

Special Forms

The different IRS forms for foreign vendors are meant to target the specific type of payee and payment. The W-8BEN is for individuals who receive income in the US. Payments to these individuals are taxable unless a tax treaty exempts the tax. W-8ECI is for companies who produce goods in the US and claim that the payments are for goods effectively connected with their US business. W-8EXP is completed by foreign governments or organizations. W-8IMY are used for payments made to an intermediary foreign flow through entity. Of these, the W-8 BEN is most common for our purposes. Any time a tax treaty is used to exempt withholding, the foreign national must also complete form 8843 to claim the treaty exemption. They should also apply for an ITIN using form W-7 when tax has to be withheld or not unless they already have an ITIN or SSN.

Assistance Available

The Shared Immigration Service is available to answer questions about any payments to foreign national individual or entities and to help determine if they are to be treated as a foreign national for tax purposes. Contact them by phone at 605-688-6949 or by email to janice.wiersma@sdstate.edu or laquita.lombard@sdstate.edu.