

Minnesota State Colleges and Universities Procedure for Withholding of Tax on Payments to Nonresident Alien Vendors

Objective

To provide Minnesota State Colleges and Universities with procedures to comply with tax laws as they apply to nonresident alien vendor payments.

Scope

This procedure is for all payments made by a Minnesota State College or University to vendors who are nonresident aliens for tax purposes. Certain immigration documents will need to be reviewed to make residency determinations, but in general immigration rules and regulations are beyond the scope of this document.

Background

In general, the IRS requires 30% federal income tax withholding on compensation paid to a foreign national¹ for independent personal services, unless the amounts are either exempt under the terms of a tax treaty, subject to a lower or reduced tax rate under the treaty, or exempt from tax under the Internal Revenue Code.

Independent personal services are services performed as an independent contractor in the U.S. by a self-employed nonresident alien rather than an employee. Compensation, including honorarium, for professional or contractor services includes (but is not limited to) the following:

- Payments for contract labor
- Payments for professional services, including fees paid to attorneys, physicians, and accountants
- Consulting fees
- Honoraria paid to visiting professors, teachers, researchers, scientists, and speakers
- Payments for performances by public entertainers
- Business expense reimbursements

The institution issuing these types of compensation payments must follow this procedure to properly report under Internal Revenue Code Section 1461. Noncompliance can result in the institution being held responsible for the payment of required federal tax withholding and penalties. Noncompliance can result in negative consequences to the foreign national as well.

Employment Eligibility: *Before* a payment can be made, the institution must determine if the payee is eligible to receive compensation. Eligibility for a nonresident alien to receive compensation from a U.S. source depends on the individual's immigration status. Immigration laws are complex and each situation must be carefully reviewed to determine what type of compensation is acceptable. **Please Contact Tax Services for guidance prior to engaging foreign vendors.** There are potential planning opportunities that may benefit all parties involved, in certain instances.

If, based on their immigration status, MnSCU determines that the foreign national is eligible to receive compensation; the payment is subject to 30% federal withholding unless legally exempted.

Procedure for Withholding of Tax on Payments (from local accounts) to Nonresident Alien Vendors

¹ A foreign national includes: nonresident alien individual, foreign corporation, foreign partnership, foreign trust, a foreign estate *and* any other person who is not a U.S. citizen.

- ☑ The department or individual intent on engaging (and making payments to or on behalf of) a nonresident alien vendor must notify the institution's business office.
- ☑ **Important: Each institution is responsible to design procedures to ensure that their business office is properly notified in advance in order to properly withhold and report. Foreign vendors shall be paid out of local bank accounts (not with State Treasury money) when withholding is required because federal withholding and reporting is currently only available when local accounts are used.**
- ☑ **Prior to authorizing vendor payments or entering into any agreement**, review and make copies of the alien individual's immigration documentation to verify that the vendor's status allows the individual to receive compensation. Gather the vendor's immigration documentation and contact Tax Services for assistance as needed.
- ☑ Responsible persons at each institution should communicate with the vendor the U.S. withholding/reporting process prior to entering into any agreement (i.e., that the appropriate tax compliance forms must be completed and that withholding may be required). Note: The general contract form for consultants has been updated to include contractual language for institutions to withhold tax on payments to nonresident aliens.
- ☑ **Tax Forms:** The nonresident alien vendor must complete and sign the MnSCU "**Vendor Tax Residency Information Form**" (the separate document is included in this material). Obtain and keep in your records the vendor signed and dated **Form W-8BEN** (Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding). Note: A vendor would complete Form W-9 (not Form W-8BEN) if they are a U.S. citizen or other U.S. person (including a resident alien individual). For a MnSCU institution to properly report payments to a nonresident alien vendor, the vendor must have either a U.S. social security number (see Form SS-5, application for U.S. social security number) or a U.S. individual taxpayer identification number (see Form W-7, application for an ITIN), unless the vendor is operating as a business entity (then see Form W-8BEN instructions). Forward a copy of the completed "Vendor Tax Residency Information Form," along with Form W-8BEN and copies of immigration documentation to Tax Services (see Office of the Chancellor contact information below). Note: Also, complete the "**B Honoraria Eligibility Certification**" form for B Visitors (example: foreign speakers) whom the institution would like to pay honoraria and/or travel expenses.
- ☑ **MAPS (Minnesota Accounting and Procurement System):** After following the steps listed above, the business office must follow these steps when setting up the vendor screen in the (MAPS) for a nonresident alien vendor. First, go into "Production Procurement." Then from the drop down menu choose "Procurement Menu (AGPS)." On the "VEND Add/Maintain" screen, complete the information as you normally would for a vendor. However, you must also enter in the "**Vendor Notes**" section the following: "**MnSCU nonresident alien vendor**" to indicate to Mn Management & Budget (MMB) personnel that this vendor is a nonresident alien for U.S. tax purposes. An "X" will then automatically appear in the "Notes Exist" box on the vendor screen.

Note: The MMB will then code this as a vendor type "10" on the Vendor Add/Maintain Finance Approval (VFIN) screen after their approval. The type 10 code has been reserved by the MMB to exclusively represent a "MnSCU nonresident alien vendor."

Also, enter the vendor TIN (FEIN/SSN) on the "VEND Add/Maintain" screen. If the foreign vendor does not have a United States TIN, then indicate "FOR" (Foreign Status) in the TIN Exempt Code.

- ☑ **Tax Treaties:** If the nonresident alien vendor is authorized to receive compensation and is a resident of a country with which the U.S. has a tax treaty, they may be eligible for tax treaty benefits. To claim a tax treaty, the vendor must complete **Form 8233**, Exemption From Withholding on Compensation for

Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual. If the payee's immigration status is that of a scholar or researcher (Q-1 or J-1), they must also attach a tax treaty statement². Note: A new Form 8233 is required each calendar year for which the vendor is claiming a treaty exemption.

- ☑ Review the Form 8233 and any attached tax treaty statement to ascertain that the information is complete and accurate. If the Form 8233 is in order and you have no reason to doubt the veracity of the information, sign and date Part IV, Withholding Agent Acceptance and Certification.
- ☑ Make copies of Form 8233 (and attached statement, if necessary) – immediately send a copy to the IRS³, keep one copy for the campus vendor files, give a copy to the vendor, and send one copy to Tax Services (see OOC contact information below).
- ☑ **Processing Nonresident Alien Vendor Payments: All payments to nonresident alien vendors must be paid from local bank accounts (not from State Treasury money – see instructions below).** When payments to the vendor are processed *and* tax is withheld, a tax check should be issued under **Vendor Account 200226791-01**. The same day the vendor payment is made the tax withholding check should be mailed to Tax Services (see OOC address below).
 - Determine the amount of federal tax to withhold per this Minnesota State Colleges & Universities procedure and/or contact Tax Services for assistance (general rule: 30% federal withholding, however review applicable treaties and immigration status).
 - Use **AC0222UG – P/O Encumbrance Liquidation** screen for encumbered amounts or **AC0210UG – Direct Payment Voucher Entry** screen for non-encumbered amounts to process a payment to the nonresident alien vendor for the amount owed less required tax withholding. Use the appropriate expense object code.
 - Use **AC0212UG – Expense Voucher Entry** screen to process an expense voucher for the amount of tax withheld using the nonresident alien's vendor number and the appropriate expense object code.
 - Use **AR0001UG – General Receipts by G/L** screen to process a cash receipt for the amount of nonresident alien vendor tax withheld. The cash receipt must be recorded to a General Ledger in the LSO appropriation and to object code 8663, Other Taxes Payable.
 - Use **AC0210UG – Direct Payment Voucher Entry** screen to process a payment to the Office of the Chancellor, Tax Services for the amount of tax withheld. Enter the General Ledger the cash receipt was recorded to and object code 8663, Other Taxes Payable.
 - Mail the local check generated from the direct payment transaction (i.e., the tax withheld) along with the Nonresident Alien Vendor Withholding/Reporting Statement to:

Minnesota State Colleges & Universities
Attn: Tax Services
30 7th Street E, Suite 350
St. Paul, MN 55101

² See IRS Publication 519, Appendix B for the text and format of the tax treaty statement to be attached to the scholar/researcher's Form 8233.

³ The IRS has 10 days in which to refuse and return unacceptable 8233's to the withholding agent. If an 8233 is returned as unacceptable, the institution must immediately begin withholding federal income tax at the rate of 30%.

If any portion of the obligation to a nonresident alien vendor resides in a State Treasury Account, follow these additional steps to reimburse the local account:

Step 1: Process a **PV1** to the **campus EFT number** using the appropriate expense object code. Again, this is done because payments to nonresident alien vendors must be paid out of local bank accounts.

Step 2: Use **AR0009UG – General Receipts by Cost Center** screen to process a cash receipt reducing the expense object code in the local bank account cost center originally charged. Expenses will be reported in the correct appropriation and fund for financial statement reporting.

- The “**Nonresident Alien Vendor Payment Reporting**” schedule must also be completed and mailed to Ann Page with the tax withholding check. On the date of vendor payment, the “Nonresident Alien Vendor Payment Reporting” schedule must also be *emailed* to Ann Page at ann.page@so.mnscu.edu.

- Recap:** First, determine if it is permissible to engage the vendor – contact Tax Services as needed. For *all* nonresident alien vendor payments, fill out the “Nonresident Alien Vendor Payment Reporting” spreadsheet with the required information and send the spreadsheet along with copies of the vendors’ employment eligibility documents (i.e. copies of the Vendor Tax Residency Information Form, Form W-8BEN, B Honoraria Eligibility Certification (if applicable), and immigration documentation), a copy of the 8233 (and any attached statement) if the vendor is claiming a tax treaty benefit, and a tax check (if withholding was applied) to OOC, Tax Services. On the day the nonresident alien vendor is paid, complete and *email* to Ann Page the “Nonresident Alien Vendor Reporting” schedule. Finally, remember to input “MnSCU nonresident alien vendor” in the MAPS vendor notes to indicate to the MMB that this is a nonresident alien vendor. And follow the instructions on how to process the nonresident alien vendor payment (ensuring the vendor is paid with *local* bank account money).

Other useful forms and publications on this topic

IRS website: www.irs.gov

IRS Publication 515, Withholding of Tax on Nonresident Aliens:
<http://www.irs.gov/pub/irs-pdf/p515.pdf>

IRS Publication 519, US Tax Guide for Aliens:
<http://www.irs.gov/pub/irs-pdf/p519.pdf>

Form SS-5, Social Security Number application
<http://www.socialsecurity.gov/online/ss-5.pdf>

Form W-7, Individual Taxpayer Identification Number application:
<http://www.irs.gov/pub/irs-pdf/fw7.pdf>

Form W-8BEN, Certificate of Foreign Status of Beneficial Owner for U.S. Tax Withholding
<http://www.irs.gov/pub/irs-pdf/fw8ben.pdf>

Form 1042-S, Foreign Persons U.S. Source Income Subject to Withholding
<http://www.irs.gov/pub/irs-pdf/f1042s.pdf>

This year end tax form will be used to report employee compensation for which a tax treaty was claimed or compensation that was paid to a nonresident alien for independent personal services, regardless of whether tax treaty benefits are claimed.

Form 8233, Exemption from Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual.
<http://www.irs.gov/pub/irs-fill/f8233.pdf>

Form 8233 is used to request tax treaty benefits on independent personal service compensation. Nonresident alien students, teachers and researchers performing dependent personal services also use Form 8233 to request tax treaty benefits.

Office of the Chancellor Tax Services Contact Information

Steve Gednalske	Tax Administrator	(651)632-5016	Steve.Gednalske@so.mnscu.edu
Ann Page	Tax Specialist	(651) 632-5007	Ann.Page@so.mnscu.edu

Mailing Address: Minnesota State Colleges & Universities, Tax Services, 30 7th Street E, Suite 350, St. Paul, MN 55101