

Seminar
NONRESIDENT EMPLOYEE TAX COMPLIANCE
Revised October 31, 1996

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LSU is required to fulfill tax reporting obligations and maintain compliance with tax and immigration laws. The Payroll Office has developed administrative procedures to comply with these obligations. This seminar is designed to share the administrative procedures that have been developed, and to work toward building a nonresident tax compliance program for the LSU System.

Identifying Nonresident Employees

Alien Tax Information Request Form

This form is used to obtain background information on a nonresident employee such as initial U.S. arrival date, visa type, anticipated departure date, number of days present in the U.S. since the initial U.S. arrival date, and if another university was attended prior to coming to LSU. The information is extremely important for monitoring the length of U.S. stay and when the substantial presence test is met. ALL NONRESIDENT ALIEN EMPLOYEES ARE REQUIRED TO COMPLETE THIS FORM. Once completed it should be forwarded to the Payroll Office.

Student Employment Data Form

Effective with first-time appointments for the 1996 Fall semester, the *Student Employment Data* form is **required** from each student employee. The form was designed to function as an employment application, as well as provide information such as citizenship, the need for an ISO work permit, if the student is on academic probation, if the student has a relationship to other LSU employees, etc. The form also incorporates the loyalty oath and acknowledgment of receipt of the drug compliance summary statement, two requirements for student employees of which many departments are not aware.

Employment Eligibility Verification (I-9) Form

All employees, citizens, and noncitizens, hired after November 6, 1986 must complete this form at the time of hire, which is the actual beginning of employment. The employer is responsible for ensuring that the form is completed. The I-9 form for student employees is sent to the Payroll Office for microfilming. The I-9 form for regular employees is maintained in the employee's HRM office.

Country Codes

The appropriate country code must be used for the nonresident employee's home country. The country code is determined and loaded on the HRM System at the time the hiring department generates the personnel form. It is extremely important that the correct country codes are used because tax treaty eligibility is determined by the country code. In addition to the forms already mentioned, the IAP-66 form and the employee's passport are two reliable source documents that will provide the employee's home country. The country code listing is provided in both alpha and numeric order (copy attached). These codes are maintained on the HRM System.

Payroll Procedures to Identify Nonresident Employees

- Run a QMF query to provide a list of all employees with country codes other than "138"- U.S. citizen.
- Once naturalized citizen documentation is provided by a nonresident employee, the country code is changed to "138".
- Once green card or resident alien card documentation is provided by a nonresident employee, the employee's record on PCON is coded "99" for "resident alien", with no change made to the country code since the employee is not a citizen of the U.S.
- Upon receipt of Alien Tax Information Request Form, code "1" on PCON to indicate the employee has completed the form.

Social Security Number

All nonresident employees must have a valid U.S. social security number. Upon hiring nonresident employees with a temporary "999" social security number that was issued by the Office of Admissions, a personnel action form may be generated. However, the forms will not be released once received in Payroll until a copy of the U.S. social security card is received. The employees **will not** be paid until they have a U.S. social security number. Therefore, if hiring an employee without a social security number, encourage them to go and apply for a U.S. social security number immediately so that their payroll check will not be delayed.

As a part of the orientation process for international students and faculty, the International Services Office arranges for a representative from the Social Security Administration Office to be available on campus one full day at the beginning of each Fall and Spring semester for any nonresident employee to apply for a social security number. The departments should always check with the ISO for the date the representative will be on campus and should provide the information to employees hired with a temporary number, and encourage them to take advantage of this service. If the employee does not apply for a social security number on campus, he/she must go to the SSA Office to complete an application.

Residency Status Determination for Tax Purposes

A "**Nonresident Alien**" for tax purposes is a person who is not a U.S. citizen and who does not possess a green card or meet the substantial presence test. There are restrictions on a nonresident alien's income tax filing status which limit the number of personal exemptions a nonresident alien is allowed. When filing the annual income tax return with the IRS, a nonresident alien **cannot** claim the standard deduction. Therefore, a W-4, Employee's Withholding Allowance Certificate, must be completed as follows:

- Check only "Single" marital status on line 3 (regardless of their actual marital status)
- , Claim only one allowance on line 5, unless the employee is from Canada, Mexico, Japan, India, or the Republic of Korea, or a U.S. national*.
- f Request an additional \$4.00 per week on line 6 except for students from India. If paid biweekly, the amount on line 6 should be \$8.00. If paid monthly the amount on line 6 should be \$16.00. The additional withholding amount applies only to federal taxes.
- „ Do not claim "Exempt" withholding status on line 7. Only students from a country with a tax treaty may claim the exemption on line 7 with the statement: "see 8233 form."

*U.S. nationals are individuals who, although not U.S. citizens, owe his or her allegiance to the United States. U.S. nationals include American Samoans and Northern Mariana Islanders who chose to become U.S. nationals instead of U.S. citizens.

There are differences that exist between the taxation of residents and nonresidents of the U.S. The basic characteristics of the nonresident taxation is as follow:

- Tax is generally levied on U.S. source income only.
- , Tax treaty provisions may exempt some income from tax.
- f Interest income may be tax free.
- „ Nonresident aliens cannot file jointly with their spouse.
- ... Generally only one personal exemption is allowed regardless of family status.
- † No standard deduction is permitted.
- ‡ Itemized deductions are limited to:
 - State and local taxes withheld
 - Contributions to charity
 - Casualty/theft losses
 - Miscellaneous business deductions
- ^ Investment income is generally taxed at a flat 30%.
- ‰ No child or dependent care credit is permitted.
- § Cannot file for Earned Income Credit

A number of special rules regarding the standard deduction and spousal exemptions are in effect for residents of India.

Indian residents should contact the IRS for additional information on these rules.

A "**Resident Alien**" for tax purposes is a person who is not a U.S. citizen and who either meets the green card test or the substantial presence test. Resident alien status is for tax purposes only and has no effect on the employees immigration status.

Green Card Test

A person is considered as having met the green card test if he/she is a lawful resident of the United States. Immigration and Naturalization Service (INS) issues an alien registration card. The first day present in the U.S. as a lawful permanent resident is considered as the residency starting date.

Substantial Presence Test

A person on an **F** or **J** student visa is considered as having met the substantial presence test after being present in the U.S. for five consecutive calendar years plus an additional 183 days in the sixth year. (typically July 3rd of the 6th year).

A person on a **J** non-student visa (researchers, scholars, teachers, etc.) is considered as having met the substantial presence test after being present in the U.S. for two consecutive calendar years plus an additional 183 days in the third year.

After being present for 183 days, a person is considered a "resident alien" for tax purposes due to meeting the substantial presence test. The residency starting date is retroactively effective as of January 1st in the year the test is met for both income and FICA taxes.

A person on an **H** visa is considered a nonresident for tax purposes until the substantial presence test is met. Meaning, the person is subject to the withholding rules for nonresident employees until present in the U.S. for 183 days.

Note: Counting the days is based on a calendar year, not a 12-month period. If the person enters the country 12/31/9X this is considered one year for counting substantial presence.

Spouse (F2/J2) visa holders are subject to the same rule for determining residency status as the employee spouse, meaning, the (F2/J2) spouse is considered a nonresident for tax purposes for the same time period as the employee spouse. **However, the (F2/J2) spouse is not exempt from FICA taxes as the employee is.**

Payroll Procedures to Determine Residency Status

• Evaluate the Alien Tax Information Request Form to determine residency status and for passage of the substantial presence test. Students (including Graduate Students)

- The visa type is loaded on PDEM screen to exempt them from FICA taxes during semester breaks and summer school if working and not enrolled in summer school.
- The visa type is not loaded for those who meet the substantial presence test so they are not exempt from FICA taxes during semester breaks and summer school if working and not enrolled in summer school.
- When the substantial presence test is met, the visa type is removed from PDEM and is coded "99" (resident alien) on the PCON screen to indicate residency status. The additional \$4 for federal withholding is also removed from the PCON screen.
- A spreadsheet is maintained to identify the students meeting the test, copies of which are provided to all Payroll Sections so that no refund of FICA is made in error.
- When a nonresident student pays FICA in error due to their visa type not loaded on PDEM, an Alien Tax Information Request Form must be completed and residency status determined before refunding the taxes. The visa type is loaded on PDEM so the student will be exempt in the future.

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Payroll Procedures to Determine Residency Status continued

Full-Time Employees

- CE HRM loads the visa type on the PDEM screen.
- When a full-time employee becomes a "resident alien," HRM codes "01/01/01" on the PDEM screen. If an individual becomes a resident alien due to passage of the substantial presence test, a letter is sent to appropriate campus HRM Office to have the employee's retirement code changed from "51- Exempt" to "49-Pay FICA".
- Ž When the retirement code is changed and the amount of FICA taxes owed is determined, an accounts receivable is established and a letter is sent to the employee informing him/her of the expired exempt visa status. The employee is subject to FICA taxes beginning January 1, if applicable, or as of the date of employment if employed after January 1.
- o Maintain an alpha file on Alien Tax Information Request Forms and a tickle file of those employees who will meet the test within the next calendar year. For regular employees as of the beginning of the year and then periodically, the pay end date is reviewed to determine if they will be employed after July 3. If so, a letter is sent to appropriate campus HRM Office to code the employee to pay FICA. If the pay end date is before July 3, no action is taken.
- o Load W-4 and L-4 Forms according to residency status determined.
- o Run query identifying the nonresident employees for tax purposes and monitor federal and state withholdings plus the additional \$4 per week.

Tax Treaties: Eligibility and Monitoring Benefits

Some countries have tax treaties with the U.S. in which all or a portion of earnings may be tax exempt. Some tax treaties provide benefits to both students and teaching/researchers, while others may only provide benefits to students or teaching/researchers and, even some may specify only teaching or researcher. Tax treaty benefits are granted based on eligibility.

- Students must initially arrive in the U.S. on an F-1 or J-1 student visa, not an F-2 or J-2. Even if they later change to an F-1 or J-1 visa after arriving on an F-2 or J-2 visa, they are not eligible.
- , Graduate assistants are always considered students, regardless of their assigned duties, and are entitled to student tax treaty benefits if from a country that provides the benefit to students.
- f Researchers, scholars, and teachers must initially arrive in the U.S. on a J-1 visa that indicates the intent or primary purpose of services to be performed.
- „ The tax treaty benefit can be granted only once and is determined by the initial intent of arrival.
- ... Eligibility for student tax treaty benefits starts in the initial year of arrival and is available generally for five taxable years. Refer to each tax treaty for expiration of benefits since each tax treaty is unique.
- † Eligibility for teaching/researcher tax treaty benefits starts in the initial year of arrival and counted on a 12-month period rather than by taxable year. (Example: PR China's teaching/researcher tax treaty benefits is available for an aggregate of three years, not three taxable years.)

Persons eligible for tax treaty benefits must complete Form 8233 and Attachment to 8233 (required additional statement). Copies of each are attached.

Payroll Procedures Relative to Granting Tax Treaty Benefits

- CE Baton Rouge campus employees eligible for tax treaty benefits are to report to the Payroll Office to complete the appropriate forms. The other campuses' HRM offices monitor eligibility and forwards forms to the Payroll Office for submission to the IRS.
- Alien Tax Information Request form is given to the employee for completion and reviewed for eligibility before the tax treaty forms are provided.
- Ž A sample form showing the required information is provided the employee as a guide.
- Upon completion, all forms are reviewed carefully to ensure acceptance by the IRS.
- The tax treaty benefit is loaded on the PCON screen with a flag "T," the appropriate income code (18 or 19), & expiring year
- ‘ The employee's country code must be verified to make sure the tax treaty will be accepted when loaded. (Example: PR China -025 and Republic of China - 126. The tax treaty is available only to those from PR China.)
- ’ The form is signed by Payroll Manager and copies are made for the IRS and for filming.
- “ A file folder containing original forms is maintained for each employee granted tax treaty benefits.

Payroll Procedures: Ineligible for Tax Treaty Benefits or Incomplete Forms

- CE Persons requesting benefits in the Payroll office who are determined to be ineligible for tax treaty benefits are provided an explanation at that time.
- The appropriate HRM office is notified when employees of their campus request tax treaty benefits and they are not eligible. The HRM office should notify the employee.
- Ž Incomplete forms or a lack of required forms results in no tax treaty benefits granted. The forms are returned to the employee for completion or to the appropriate HRM office if not employed on the BR campus.

Upon completion of the tax treaty forms a copy is sent to the IRS for review and approval. A waiting period of 10 days must elapse before the tax treaty benefit can be granted, therefore, the tax treaty forms are held in a pending folder until the 10 day period has elapsed. If the employee is due to be paid during the 10 day period, income taxes are withheld according to the rules for withholding discussed earlier for nonresident aliens. If the IRS determines the employee to be ineligible, the employee is informed of his/her ineligible status. After the 10 day period elapses and there is no ineligible notice from the IRS, the tax treaty benefit is granted to the employee.

Tax treaties expire every December 31. New forms must be completed and the eligibility is again reviewed to verify that the tax treaty benefits can be continued. The Payroll Office holds a two-day "Open House" in November to assist with the renewal of tax treaty benefits. As soon as the dates are set, the information is published in the Accounting Services newsletter. Flyers are sent to departmental personnel handling payroll, and a list is sent to departments identifying those who may be eligible for continued tax treaty benefits. The employees identified on the list are advised to take advantage of this service provided by the Payroll Office.

Tax Treaty Facts (attached) is a summary listing of all tax treaties currently in effect and indicates the type of employee for which the treaty applies. The country's assigned country code, maximum period allowed under the tax treaty, maximum exemption amount, and the tax treaty article number are pertinent information related to the tax treaties that are important for employees to know and are needed for filing income tax returns. These are fields in the HRM/Payroll System to monitor tax treaty earnings and compliance with specified amounts.

Nonresident Student Employees

Valid Work Permit

Departments should always make sure before hiring nonresident alien students that the students have a valid work permit. The International Services Office will determine eligibility to work and will provide the work permit to the students. The departments should review the work permit at the beginning of each semester to make sure their student is still eligible to work. The students should not begin employment prior to the date of their work permit, because they can only be paid for hours worked starting with or after the effective date of the work permit.

Work Hours Limited to 20

Nonresident alien student employees with an F-1 or J-1 visa are only allowed to work 20 hours per week when classes are in session. The Payroll Office and the Student Aid Office monitor the hours worked and identify those students who have exceeded 40 hours in a pay period. Any violation of this requirement which has been set by the Immigration and Naturalization Service will result in the following action:

1st violation: The student will receive an initial warning letter to monitor hours worked.

2nd violation: The student will receive a one-week suspension from work.

3rd violation: ISO will revoke the work permit and the student will not be able to work for the remainder of the semester.

Both departmental supervisors and the ISO will receive copies of letters sent to the students informing them of any violations. Attached is a copy of the report provided by Student Aid to indicate the nonresident students' work hours for the pay period. Also, attached is a sample letter sent to the employee, department, and ISO.

FICA Tax Exemption

All student employees (U.S. citizens and nonresidents) are exempt from paying FICA taxes during regular semesters. However, the FICA exemption is not available during semester breaks and if working during the summer and not enrolled in summer school. Those nonresident students who are considered "exempt individuals" (less than five years in U.S.) are granted the FICA tax exemption during semester breaks and if working but not enrolled in summer school.

International Service Office (ISO)

The ISO hosts an orientation for all new nonresident students and employees at the beginning of the Fall and Spring semester. Payroll participates to provide information to those students who intend to work on campus. Materials containing pertinent information are provided to the students. A sample handout is attached.

Yearend Reporting

Nonresident employees who claimed tax treaty benefits during the year will receive Form 1042-S. Form 1042-S is required by the IRS to report earnings paid to a nonresident alien that are exempt from federal withholding due to a tax treaty. Form W-2 only reports earnings that are subject to federal withholdings.

The Payroll Office is not responsible for filing the annual Form 1042 with the IRS, but does have a responsibility for those individuals paid through Payroll that receives a Form 1042-S. The Accounts Payable Division of Accounting Services has the responsibility of filing the annual Form 1042-S and remitting the federal withholdings. Form 1042-S is required to be furnished to the recipient of income by March 15th. Also, March 15th is the IRS deadline for forms 1042-S and 1042.

Form 1042-S is required by the IRS to report tax treaty earnings, nonresident fellowships and scholarships, nonresident royalty income, etc.. The following income codes must be used for the associated income:

- 19 - Student Tax Treaty Earnings
- 18 - Teaching/Researcher Tax Treaty Earnings
- 15 - Scholarships/Fellowships
- 16 - Independent Personal Services
- 12- Royalties

The following codes are used to determine authority for exemption:

- 02 - Exempt under an Internal Revenue Code provision
- 03 - Income is not from U.S. sources
- 04 - Exempt under tax treaty

Nonresident fellows receiving a fellowship and from a country with a tax treaty must complete Form 1001 (see sample attached) to be exempt from the required federal withholding at 14%. Nonresident fellows receiving a fellowship from countries without tax treaties are not exempt from the 14% federal withholding.

Nonresident employees who also had income subject to income taxes will receive a W-2, which is required by the IRS to report only taxable wages. The W-2 form must be distributed by January 31.

Nonresident employees are required to submit both a 1040NR and Form 8843 to the IRS by April 15. The Payroll Office conducts a seminar in the Spring Semester to provide general information to employees for filing their returns.

The IRS publishes two brochures of interest to nonresident aliens: Publication 519, Tax Guide for Aliens, and Publication 901, Tax Treaties. A copy of each is attached. Please read and be familiar with the information contained in these publications.

Payroll Procedures: Form 1042-S / Form 1042

- OE Maintains ledgers and balances nonresident tax withholding.
- Processes monthly journal vouchers, by employee name and SSN, to transfer the federal tax withholdings to a specified account number in the Accounts Payable Division to be remitted to the IRS.
- Z Maintains spreadsheet of employees due to receive Form 1042-S for fellowship earnings subject to 14% tax, living expense reimbursement considered income, etc.

Lowell G. Hancock
Internal Revenue Agent
International Issue Specialist

Mr. Hancock has been very helpful in answering various questions regarding our nonresident employees. Often Mr. Hancock is consulted for verifying information when employees disagree with an interpretation made by Payroll. Those employees who choose to pursue their argument further are told that they must provide written documentation on IRS letterhead before our interpretation is changed.

Mr. Hancock provided documentation he uses to educate IRS agents for university audits of nonresident employees. A copy of the documentation which outlines the responsibility of the university is attached for your review. If you can access information requested in Mr. Hancock's document through your payroll system, you have reached the goal of establishing compliance for nonresident employees.

Contact Mr. Hancock with questions at:

In Akron:

Internal Revenue Service
Federal Bldg/U.S. Courthouse
2 S Main St., Rm 395
Akron, Ohio 44308-1869

Telephone (330) 375-5421
FAX (330) 375-5507

In Washington, D.C.

Internal Revenue Service
Assistant Commissioner (International)
Foreign Payments Division
950 L'Enfant Plaza South SW
Washington, D.C. 20024

Telephone (202) 874-1800
FAX (202) 874-1883
VMS 6280163419
E-Mail LHANCOCK@PRODIGY.COM

Attachments

1. Alien Tax Information Request
2. Student Employment Data
3. Form I-9
4. SPICDE screen - Country Codes are updated by System Office
5. Country Code Listings
6. HRM PCON screen - Sample "Resident Alien" Employee coded 99
7. Form W-4 sample
8. Tax Treaty Packet
 - Attachment to Form 8233
 - Form 8233
 - Form W-4
 - Form L-4
9. Form 8233 sample - Baker & McKenzie: Nonresident Alien Tax Compliance
10. HRM Code Tables Menu screen and
Tax Treaty Code Tables screen - update Tax Treaty additions/deletions
11. PCON & PBAL screens - Sample of a student employee coded w/tax treaty benefit
12. PBAL screen - Sample of graduate student with maximum exemption limit
reached and subject to income tax.
13. Tax Treaty Facts
14. Form 8233 - blank form
15. Attachments to Form 8233 - required additional statement for each tax treaties
16. International Students Work Hours over 40 - Sample report provided by Student Aid Office
& Sample Letter sent by Payroll to Students, Department, and ISO
17. International Student Orientation - Sample handout for ISO orientation
18. Form 1042-S
19. Form 1001
20. IRS Handout from Lowell Hancock - University Responsibilities With Respect to Employee
Wages Paid to Aliens
21. Activity Schedule: Payroll Processing Procedures for Nonresident Alien Employees