



MANUAL TRANSMITTAL

Department of the Treasury
Internal Revenue Service

4.10.21

MARCH 23, 2023

EFFECTIVE DATE

(03-23-2023)

PURPOSE

- (1) This transmits revised IRM 4.10.21, Examination of Returns, U.S. Withholding Agent Examinations – Form 1042.

MATERIAL CHANGES

- (1) IRM 4.10.21.1, Program Scope and Objectives: Updated policy owner to ADCCI, SPG, Policy Office.
- (2) IRM 4.10.21.1, Program Scope and Objectives: Updated program owner to the Foreign Payments Practice under Withholding Exchange & International Individual Compliance Practice Area.
- (3) IRM 4.10.21.7.1.4, Limitation of Benefits (LOB): Updated IRM references to IRM 4.60.2 and IRM 4.60.3 due to updates to those IRM sections.
- (4) IRM 4.10.21.8.1: Updated title for improved clarity.
- (5) IRM 4.10.21.8.1.7: Updated title and instructions to better identify the submission address is for original delinquent tax returns under Voluntary Disclosure Procedures.
- (6) Exhibit 4.10.21-4, Sample IDR for Audits of Financial Services Companies: Replaced the table with an updated graphic to conform with IRM 2.30.1, Section 508 Compliance.
- (7) Exhibit 4.10.21-5, Sample IDR for Audits of Nonfinancial Services Companies: Replaced the table with a graphic to conform with IRM 2.30.1, Section 508 Compliance.
- (8) Updated the Director of Field Operations, (FPP), to the Director of Field Operations, (FPP) & (AEOI), throughout.
- (9) Editorial and grammatical changes made throughout.

EFFECT ON OTHER DOCUMENTS

This IRM supersedes IRM 4.10.21 dated August 29, 2019.

AUDIENCE

LB&I employees

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4.10.21

U.S. Withholding Agent Examinations - Form 1042

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4.10.21.1
(03-23-2023)
Program Scope and Objectives

- (1) **Purpose** – This IRM section provides the basic concepts on determining the type of income subject to certain U.S. withholding and reporting requirements, specifically with respect to withholding under IRC 1441-1443 (NRA withholding). It also provides general guidance on examining Form 1042, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons, with respect to NRA withholding.
 - a. This IRM will cover basic concepts related to NRA withholding. This IRM will not cover in detail withholding and reporting requirements under Chapter 4 (IRC 1471 - 1474), commonly referred to as the Foreign Account Tax Compliance Act or FATCA.
 - b. IRM 4.10.21.2 provides a description of the NRA withholding tax; IRM 4.10.21.3 provides a summary of relevant Code sections; and IRM 4.10.21.4 provides a brief comparison of backup withholding to the NRA withholding tax.
 - c. IRM 4.10.21.5 provides a brief comparison of FATCA withholding to the NRA withholding tax.
 - d. IRM 4.10.21.6 describes important forms to know related to NRA withholding. IRM 4.10.21.7 describes treaty benefit requirements.
 - e. This IRM will cover two types of U.S. withholding agent audits. IRM 4.10.21.9 will provide general guidance for audits of U.S. financial institutions, which may have Nonresident Alien (NRA) withholding tax and reporting requirements in connection with their custodial or brokerage activities. IRM 4.10.21.10 will provide general guidance for audits of U.S. non-financial entities that may have NRA withholding and reporting responsibilities with respect to their payments to foreign persons.
 - f. This IRM will not discuss the qualified intermediary (QI, see definition below) periodic reviews required under the QI Agreement between the QI and the IRS. See Rev. Proc. 2017-15.
- (2) **Audience** – LB&I employees who conduct Form 1042 examinations will be the primary users of this IRM.
- (3) **Policy Owner** – LB&I Policy under the Strategy, Policy and Governance office in the Assistant Deputy Commissioner Compliance Integration organization.
- (4) **Program Owner** – The Foreign Payments Practice under Withholding Exchange & International Individual Compliance Practice Area.
- (5) **Primary Stakeholders** – Internal or external offices or functions whose employees are responsible for following or developing these procedures.
- (6) **Program Goals** – FPP provides oversight of nonresident alien withholding tax matters with an emphasis on Servicewide coordination of technical issues, compliance, processing and other information relating to nonresident aliens.

4.10.21.1.1
(09-20-2018)
Background

- (1) Generally, a foreign person is subject to U.S. tax on its U.S. source income. Most types of U.S. source fixed or determinable annual or periodical (FDAP) income received by a foreign person are subject to U.S. tax of 30%. A reduced rate, including exemption, may apply if an Internal Revenue Code section provides for a lower rate, or there is a tax treaty between the foreign person's country of residence and the United States. The tax is generally withheld (NRA withholding) from the payment made to the foreign person. The term "NRA

withholding” is used in this IRM to refer to withholding under IRC 1441 - 1443 and does not include other Chapter 3 withholding (for example under IRC 1445 or 1446).

- (2) Certain payments of U.S. source FDAP income may be subject to withholding under Chapter 4 (FATCA withholding) rather than Chapter 3. If FATCA withholding applies to a payment, NRA withholding does not. This IRM has been updated to include limited concepts related to FATCA withholding that are needed to understand NRA withholding; however, it generally does not cover withholding and reporting requirements under Chapter 4.
- (3) A withholding agent examination is performed to ensure that all applicable payments made to nonresident aliens and foreign corporations have been properly reported, withheld, and paid under Chapter 3 or 4. A withholding agent is any person that has control, receipt, custody, disposal, or makes payment of U.S. source FDAP income of a foreign person that is subject to NRA withholding or FATCA withholding.

Note: A payment may be reportable even if it is not withholdable.

- (4) A withholding agent must obtain a withholding certificate (see IRM 4.10.21.6) prior to a payment being made except if the payment is one for which the withholding agent may obtain documentary evidence (in general, payments made outside the United States). The withholding agent generally relies upon this withholding certificate to determine the payee’s status as a U.S. or foreign person, their recipient type (individual, corporation, etc.), their Chapter 4 status (if applicable), and the payee’s claim for relief from or a reduced rate of withholding under a tax treaty. If a withholding agent does not secure a valid withholding certificate that the withholding agent is permitted to rely upon under the due diligence standards (see IRM 4.10.21.7.2; and IRM 4.10.21.9.3), the presumption rules should be applied (see IRM 4.10.21.9.3.3). A withholding agent that makes payments of U.S. source FDAP income required to be reported on Form 1042-S is required to file Form 1042, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons, to report these payments. A withholding agent also needs to file Form(s) 1042-S, Foreign Person’s U.S. Source Income Subject to Withholding, to report the payment and withholding to the payees. Form 1042-S is an information return that reports each income type to each payee, which is to be filed with the IRS, with a recipient copy furnished to the payee.
- (5) An examination should verify that all payments subject to reporting and withholding are identified, withheld upon if necessary, paid to the U.S. Treasury, and that required forms are properly and timely filed with the IRS. An examiner should look at various payment streams (such as vendor payments, treasury, and custodial) to ensure that all applicable payments are captured by the reporting system used to compile Form 1042 reporting. Internal controls should also be reviewed to verify that systems and procedures were in place to meet Chapter 3 and 4 requirements.

4.10.21.1.2
(09-20-2018)
Authority

- (1) IRC 1441-1443 and 1461 set forth when and how the tax is required to be withheld and reported. Treas. Reg. 1.1441-2 prescribes certain additional exceptions to when withholding is required under Chapter 3.

4.10.21.1.3
(03-23-2023)
Responsibilities

- (1) The Director of Field Operations, Foreign Payments Practice (FPP) & Automatic Exchange of Information (AEOI) is the executive responsible for the withholding program.
- (2) The Director of Field Operations, FPP & AEOI is responsible for composition reviews involving maintaining, numbering, formatting, and processing the IRM for FPP.
- (3) The Director of Field Operations, FPP & AEOI is also responsible for planning, developing, coordinating, administering and evaluating the policies, systems, procedures and standards for FPP.

4.10.21.1.4
(03-23-2023)
Program Management and Review

- (1) **Program Reports** – The Director of Field Operations, FPP & AEOI monitors changes to the IRM and reports on potential areas of risk to the IRS. IBMIS, ACIS, ERCS, and AIMS reports are used to support program objectives.
- (2) **Program Effectiveness** – Program goals are evaluated by annual assurance reviews (FMFIA).

4.10.21.1.5
(09-20-2018)
Program Controls

- (1) Program goals are reviewed by executives and evaluated based on annual commitments of LB&I priorities.

4.10.21.1.6
(09-20-2018)
**Terms/Definitions/
Acronyms**

- (1) See Exhibit 4.10.21-1 for a list of terms and definitions. See the table below for frequently used acronyms.

Acronyms

Acronym	Definition
ECI	Effectively Connected Income
FDAP	Fixed, Determinable, Annual or Periodical
NRA	Nonresident Alien
QI	Qualified Intermediary

4.10.21.1.7
(03-23-2023)
Related Resources

- (1) For further assistance, contact the Foreign Payments Practice Network. Also see **U.S. Withholding Agent Program** at <https://www.irs.gov/businesses/international-businesses/us-withholding-agent-program>; and **Tax Treaties** at <https://www.irs.gov/individuals/international-taxpayers/tax-treaties>.

4.10.21.2
(09-20-2018)
NRA Withholding Tax

- (1) Certain income received or deemed received by foreign persons is subject to United States taxation on a gross basis. The income must be fixed, determinable, annual or periodical (FDAP); it must be U.S. sourced; and it must not be included in the foreign person's gross income as effectively connected with any U.S. trade or business of that person (ECI). If these conditions are met, the income will generally be subject to the withholding rate under IRC 1441 or IRC 1442 (generally 30%) – generally referred to as nonresident alien (NRA) withholding. The withholding rate can be reduced or eliminated based on an applicable treaty or Code section, such as the portfolio interest exception.

- (2) Withholding and reporting might instead be required under IRC 1445 with respect to dispositions of U.S. real property interests and under IRC 1446 with respect to partnerships' allocation of ECI to foreign partners. Withholding under these sections is not included in the definition of NRA withholding for purposes of this IRM section.

4.10.21.3
(09-20-2018)

**Summary of Relevant
Code Sections**

- (1) IRC 1441 - generally sets forth such things as:
- The persons subject to having NRA withholding applied against their income
 - The income subject to withholding
 - The entities qualifying as withholding agents
 - The statutory withholding rates
- (2) IRC 1442 - requires the withholding of tax in certain cases with respect to payments made to foreign corporations.
- (3) IRC 1443 - requires the withholding of tax in certain cases with respect to foreign tax- exempt organizations and prescribes the 4% withholding rate applicable to foreign private foundations.
- (4) IRC 1461 - sets forth a withholding agent's liability for under-withheld tax.
- (5) IRC 1463 - allows for the application of interest and penalties to cases in which the payee paid the underlying tax that was required to have been withheld.
- (6) IRC 871(a) and IRC 881 - provide for the imposition of tax on certain U.S. source income paid to nonresident alien and foreign corporations who are not engaged in a U.S. trade or business.

4.10.21.4
(09-20-2018)

**Form 1099 Backup
Withholding Tax vs. NRA
Withholding Tax**

- (1) The Form 1099 / Backup Withholding and NRA Withholding Tax regimes share some basic similarities. Both systems require the reporting of certain types of income and the withholding of taxes in certain cases. Both have an annual income tax return requirement, which is Form 945 with respect to backup withholding during the calendar year and Form 1042 with respect to reporting certain U.S. source payments made to foreign persons and amounts withheld (including NRA withholding). In addition, both have informational reporting requirements with respect to income recipients (Forms 1099 and Forms 1042-S for U.S. and foreign recipients, respectively). Apart from these separate reporting requirements, withholding and reporting occurs under these regimes based on different criteria. As a result, despite some general similarities, a major determination for a withholding agent is in properly documenting or otherwise classifying a recipient as either a U.S. or a foreign person. When a recipient is a U. S. person, NRA withholding is inapplicable, and Form 1099 reporting and backup withholding is sometimes required. When a recipient is foreign person, NRA withholding and reporting is required (or, if the foreign person is an entity, FATCA withholding may be required) with respect to certain income payments, and no Form 1099 / backup withholding requirements are triggered. For further guidance on backup withholding, see IRC 3406 and Pub 1281.
- (2) Although this IRM section deals principally with NRA withholding, Form 1099 reporting and backup withholding also needs to be considered as part of an integrated audit. Auditing Form 1042 information can result in collateral adjust-

ments to Forms 1099 and 945 when, for example, persons classified as foreign by a withholding agent need to be reclassified as U.S. persons subject to backup withholding and Form 1099 reporting. Additionally, deficiencies in a withholding agent's Form 1042 related systems may indicate a generic problem in its tax reporting systems.

4.10.21.5
(09-20-2018)
**FATCA Withholding vs.
NRA Withholding Tax**

- (1) Chapter 4 (IRC 1471 - 1474), commonly referred to as "FATCA", was added to the Code in 2010. While the purpose of FATCA is to obtain information reporting with respect to U.S. taxpayer's foreign financial accounts, certain payments of U.S. source FDAP income (withholdable payments) to foreign financial institutions (FFIs) and nonfinancial foreign entities (NFFE) may be subject to withholding under Chapter 4 (FATCA withholding). If a withholding agent applies FATCA withholding to a withholdable payment, NRA withholding will not apply.
- (2) A rate of 30% applies to withholdable payments that are subject to FATCA withholding (IRC 1471(a) and 1472(a)). Under IRC 1473(1), the term "withholdable payment" means a payment of certain U.S. source FDAP income. U.S. source FDAP income for purposes of Chapter 4 is similar to that of Chapter 3, with some exceptions (notably for nonfinancial payments such as payments for services). For payments not treated as withholdable payments, see Treas. Reg. 1.1473-1(a)(4).

Note: If a withholdable payment is made to a recipient that is a U.S. person, Form 1099/backup withholding requirements may be triggered.

- (3) In addition to NRA withholding, a withholding agent also must report on Form 1042 (and Forms 1042-S) any withholdable payments with respect to which FATCA withholding is applied. A withholding agent's obligation to file Forms 1042 and 1042-S are described in Treas. Reg. 1.1474-1(c) and (d).
- (4) Although this IRM section deals principally with NRA withholding, FATCA withholding also needs to be considered as part of an integrated audit. Auditing Form 1042 information should include both NRA withholding and FATCA withholding. Contact the Foreign Payments Practice Network for more information about FATCA withholding issues that relate to Form 1042.

4.10.21.6
(09-20-2018)
**Important Forms to
Know**

- (1) **Form 945 – Annual Return of Withheld Federal Income Tax** (See IRM 4.10.21.6.1, Tax and Information Returns, and Instructions for Form 945, Annual Return of Withheld Federal Income Tax.)
- (2) **Form 1042 – Annual Withholding Tax Return for U.S. Source Income of Foreign Persons** (See IRM 4.10.21.6.1, Tax and Information Returns, and Instructions for Form 1042, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons.)
- (3) **Form 1042-S – Foreign Person's U.S. Source Income Subject to Withholding** (See IRM 4.10.21.6.1, Tax and Information Returns, and Instructions for Form 1042-S, Foreign Person's U.S. Source Income Subject to Withholding.)
- (4) **Forms 1099 – Information returns for various types of payments to U.S. persons** (See IRM 4.10.21.6.1, Tax and Information Returns; General Instructions for Certain Information Returns (Forms 1096, 1097, 1098, 1099, 3921, 3922, 5498, and W-2G); and specific instructions for the appropriate form

required for the type of payment, e.g., Form 1099-DIV for dividends and distributions, Form 1099-INT for interest, Form 1099-MISC for miscellaneous income, etc.)

- (5) **Form 8233 – Exemption From Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual** (See IRM 4.10.21.6.2, Withholding Certificates, and Instructions for Form 8233, Exemption from Withholding on Compensation for Independent (and Certain Dependent) Personal Service of a Nonresident Alien Individual.)
- (6) **Form W-8BEN – Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Individuals)** (See IRM 4.10.21.6.2, Withholding Certificates; Instructions for Form W-8BEN, Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Individuals); and Instructions for the Requester of Forms W-8BEN, W-8BEN-E, W-8ECI, W-8EXP, and W-8IMY.)
- (7) **Form W-8BEN-E – Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities)** (See IRM 4.10.21.6.2, Withholding Certificates; Instructions for Form W-8BEN-E, Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities); and Instructions for the Requester of Forms W-8BEN, W-8BEN-E, W-8ECI, W-8EXP, and W-8IMY.)
- (8) **Form W-8ECI – Certificate of Foreign Person’s Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States** (See IRM 4.10.21.6.2, Withholding Certificates; Instructions for Form W-8ECI, Certificate of Foreign Person’s Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States; and Instructions for the Requester of Forms W-8BEN, W-8BEN-E, W-8ECI, W-8EXP, and W-8IMY.)
- (9) **Form W-8EXP – Certificate of Foreign Government or Other Foreign Organization for United States Tax Withholding and Reporting** (See IRM 4.10.21.6.2, Withholding Certificates; Instructions for Form W-8EXP, Certificate of Foreign Government or Other Foreign Organization for United States Tax Withholding and Reporting; and Instructions for the Requester of Forms W-8BEN, W-8BEN-E, W-8ECI, W-8EXP, and W-8IMY.)
- (10) **Form W-8IMY – Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities)** – (See IRM 4.10.21.6.2, Withholding Certificates; Instructions for Form W-8IMY, Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities); and Instructions for the Requester of Forms W-8BEN, W-8BEN-E, W-8ECI, W-8EXP, and W-8IMY.)
- (11) **Form W-9 – Request for Taxpayer Identification Number and Certification** (See IRM 4.10.21.6.2, Withholding Certificates, and Instructions for the Requester of Form W-9, Request for Taxpayer Identification Number and Certification.)

4.10.21.6.1
(09-20-2018)
**Tax and Information
Returns**

- (1) **Form 1042 – Annual Withholding Tax Return for U.S. Source Income of Foreign Persons.** This is the income tax return for reporting the liability for NRA withholding tax or Chapter 4 withholding, the amounts withheld, the amounts subject to reporting or withholdable payments paid to foreign persons and any credit claimed for amounts withheld by other withholding agents. This

return is due on March 15th (or the next business day if the 15th falls on a nonbusiness day) of the following year. All Forms 1042 are required to be filed on a calendar year basis, and consolidation of separate legal entities for Form 1042 filing purposes is NOT permitted. For Forms 1042 filed on or before April 15 following the end of the calendar year covered by the Form, the Form 1042 is considered filed on April 15 for purposes of determining the statute of limitations on assessment. See IRC Section 6501(b)(2).

- (2) **Form 1042-S** – Foreign Person’s U.S. Source Income Subject to Withholding. This is an information reporting form that a withholding agent files with the IRS and issues to each foreign recipient that receives an amount subject to reporting or withholdable payment. It shows, among other things, the amount and type of income paid to the recipient, the tax withheld, and any applicable withholding exemption. The Form(s) 1042-S have the same due date as the Form 1042 (generally excluding filing extensions) for filing with the IRS and for furnishing copies to the recipients.

Note: Certain information the foreign entity provides in the Form W-8 BEN-E should correspond and be consistent with information the withholding agent provides in the recipient’s Form 1042-S, for example, recipient’s Ch. 3 status code, Ch. 4 status code, LOB code, country code, income code, exemption code, tax rate, address, U.S. TIN, foreign TIN, and GIIN, if any.

- (3) **Form 945** – This form, Annual Return of Withheld Federal Income Tax, is used to report withheld federal income tax from certain nonpayroll payments, including gambling, IRAs and pensions. Another type of nonpayroll payment is backup withholding. Backup withholding is generally required when a payor does not have a valid U.S. tax identification number (TIN) for a U.S. person receiving certain types of payments that are subject to 1099 reporting. See Pub 15 and Pub 1281 for more information on Form 945.

- (4) **Form 1099** means:

- a. **Form 1099-B**, Proceeds from Broker and Barter Exchange Transactions
- b. **Form 1099-DIV**, Dividends and Distributions
- c. **Form 1099-INT**, Interest Income
- d. **Form 1099-MISC**, Miscellaneous Income
- e. **Form 1099-OID**, Original Issue Discount

and any other form in the IRS Form 1099 series appropriate to the type of payment required to be reported with respect to certain U.S. persons.

4.10.21.6.2
(09-20-2018)

Withholding Certificates

- (1) **Form W-8BEN** – Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Individuals)
- a. This form is provided by non-U.S. individuals to certify that they are foreign individuals, that they are the beneficial owner of the income, and that the income received (or to be received) by such individuals is not effectively connected with the conduct of a U.S. trade or business. It may also be used to claim withholding related treaty benefits when properly completed. A Form W-8BEN also may be used by an individual to document its Chapter 4 status. See Exhibit 4.10.21-6 for validity period rules.
 - b. This form may be used to substantiate claims of a reduced rate of withholding or exemption pursuant to the Internal Revenue Code.

- c. Note that prior to 2014, Form W-8BEN (Revision date February 2006) was available to both individuals and entities. With the February 2014 revision, Form W-8BEN was updated to only be used by individuals. The 2006 version of Form W-8BEN was in effect for foreign entities until December 31, 2014. Withholding agents that obtained the 2006 version of the Form W-8BEN prior to January 1, 2015 are able to rely on that form, for Chapter 3 purposes, until the form expires.
- (2) **Form W-8BEN-E** – Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities)
 - a. This form is provided by non-U.S. entities to certify that they are foreign entities, that they are the beneficial owner of the income, and that the income received (or to be received) by such entities is not effectively connected with the conduct of a U.S. trade or business. It may also be used to claim withholding related treaty benefits when properly completed. A Form W-8BEN-E also may be used by an entity to document its Chapter 4 status. See Exhibit 4.10.21-6 for validity period rules.
 - b. This form was created in 2014 as a form separate from Form W-8BEN. Prior to 2014, Form W-8BEN (Revision date February 2006) was available to both individuals and entities. The first version of Form W-8BEN-E was dated February 2014.
- (3) **Form W-8IMY** – Certificate of Status of Beneficial Owner for United States Tax Withholding and recipient that is an intermediary or flow-through entity, rather than itself a beneficial owner of the income being paid to it. This form is commonly used by foreign financial institutions such as broker-dealers that are receiving payments in an intermediary capacity on behalf of their account holders. See Exhibit 4.10.21-6 for validity period rules.
- (4) **Form W-8ECI** – Certificate of Foreign Person's Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States. This form is provided to a withholding agent by a foreign recipient who is the beneficial owner of a reportable amount or withholdable payment, to certify that the income received (or to be received) is ECI that the recipient is to report on a U.S. income tax return (i.e., Form 1120F or Form 1040NR). Although no tax needs to be withheld in such cases, there is a Form 1042-S reporting requirement imposed on the withholding agent. See Exhibit 4.10.21-6 for validity period rules.
- (5) **Form W-8EXP** – Certificate of Foreign Government or Other Foreign Organization for United States Tax Withholding and Reporting –This form is provided to a withholding agent by a foreign recipient who is the beneficial owner of the reportable amount or withholdable payment claiming certain withholding exemptions or reduced rates. A common use of this form is when the recipient is a foreign government or foreign tax-exempt organization. Although there generally will be no withholding tax (see exception for foreign private foundations which are generally subject to 4% withholding tax under Treas. Reg. 1.1443-1(b)), there generally will be Form 1042-S reporting of the reportable amounts or withholdable payment. See Exhibit 4.10.21-6 for validity period rules.
- (6) **Form W-9** – Request for Taxpayer Identification Number and Certification – This form is used for certifying a recipient's status as a U.S. person and providing their U.S. tax identification number. No Chapter 3 or 4 withholding

and reporting is required in such cases (see above concerning Form 1099 / Backup Withholding). For purposes of Chapters 3 and 4, this form must be retained for three years from the date the account is opened.

- (7) **Form 8233** – Exemption From Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual – This form is completed by a nonresident alien individual to obtain a tax treaty withholding exemption with respect to amounts paid for the individual's performance of certain personal services within the U.S. This form should be completed and submitted to the withholding agent on an annual basis.

4.10.21.6.3
(03-23-2023)

**U.S. or Foreign Taxpayer
Identification Number (or
Global Intermediary
Identification Number)
Requirements for
Withholding Certificates**

- (1) In certain circumstances, a Form W-8 must include the account holder's U.S. Taxpayer Identification Number (TIN) in order for such form to be valid. For example, a U.S. TIN is required on a Form W-8BEN-E if the form is being provided to claim treaty benefits or on a Form W-8ECI if the form is being provided by an entity in certain cases. See Treas. Reg. 1.1441-1(e)(4)(vii) for additional information as to when a U.S. TIN is required.
- (2) There are some exceptions for requiring a U.S. TIN on a Form W-8BEN or Form W-8BEN-E used for a treaty claim. One of the main exceptions is when the form includes a treaty claim and the beneficial owner provided its foreign TIN in lieu of its U.S. TIN. See Treas. Reg. 1.1441-6(c)(1) for the exceptions to requiring a U.S. TIN.
- (3) If the Form W-8 is being provided by the account holder with respect to a financial account (as defined in Treas. Reg. 1.1471-5(b)) held at a U.S. office of a financial institution (including a U.S. branch of a foreign financial institution (FFI)), the Form W-8 must include the TIN issued to the account holder by its jurisdiction of tax residence unless:
- a. The account holder has not been issued a TIN.
 - b. The jurisdiction does not issue TINs; or if the account holder is an entity that identified itself as a government, central bank of issue, or international organization, or if the entity is a resident of a U.S. possession.

Note: If a foreign TIN is not provided and the entity is not a government, central bank of issue, international organization, or a resident of a U.S. possession, it must provide the withholding agent with a reasonable explanation as to why it is not providing a foreign TIN. For this purpose, a reasonable explanation includes a statement that the entity is not legally required to obtain a TIN in its jurisdiction of tax residence. Such explanation may be written on the form itself (on Line 6, foreign TIN), in the margin of the form, or on a separate attached statement associated with the form. See Notice 2017-46 for the years for which foreign TINs and dates of birth are required on Forms W-8 and for exceptions to this requirement.

- (4) If a Form W-8BEN-E, W-8IMY, or W-8EXP is provided by an entity that has certain Chapter 4 statuses (including participating FFI, registered deemed-compliant FFI, direct reporting NFFE, and sponsored direct reporting NFFE), the withholding agent is required to obtain and verify the entity's Global Intermediary Identification Number (GIIN). The entity's GIIN is verified against the published IRS FFI list. (See Instructions for the Requestor of Forms W-8BEN, W-8BEN-E, W-8ECI, W-8EXP, and W-8IMY).

- 4.10.21.6.4
(09-20-2018)
Limitations on Benefits (LOB)
- (1) Part III (Claim of Tax Treaty Benefits) of the Form W-8BEN-E has checkboxes listing each of the main tests that can be met to satisfy an LOB provision under a particular income tax treaty. In addition, there is also a checkbox provided for an entity to indicate if it obtained a favorable discretionary determination from the U.S. competent authority that it qualified for the treaty benefits associated with the Form W-8BEN-E being provided. (See Instructions for Form W-8 BEN-E.) The Form 1042-S has a box to list the LOB code corresponding to a LOB checkbox on the Form W-8BEN-E.
- 4.10.21.6.5
(09-20-2018)
Validity
- (1) A Form W-8BEN-E will remain valid for purposes of both Chapters 3 and 4 for a period starting on the date the form is signed and ending on the last day of the third succeeding calendar year, unless a change in circumstances makes any information on the form incorrect (see Form W-8BEN-E instructions). However, under certain conditions a Form W-8BEN-E will remain in effect indefinitely until a change of circumstances occurs. To determine the period of validity for Form W-8 BEN-E for purposes of Chapter 4, see Treas. Reg. 1.1471-3(c)(6)(ii). To determine the period of validity for Form W-8BEN-E for purposes of Chapter 3, see Treas. Reg. 1.1441-1(e)(4)(ii) and see Exhibit 4.10.21-6. The indefinite exception does not apply to the portion of the form that includes a treaty claim, as a treaty claim is always subject to the general 3-year validity rule.
- 4.10.21.7
(09-20-2018)
Treaty Benefit Requirements
- (1) This IRM subsection provides a high-level overview of the requirements, including limitation of benefits, that a foreign person must meet to claim treaty benefits. Additionally, information is provided in this subsection concerning the due diligence withholding agents must perform to verify the accuracy of treaty claims.
- (2) This subsection also provides guidance as to what examiners should look for as part of a Form 1042 examination, regarding withholding agent's application of the due diligence standards related to the verification of treaty claims made by foreign entities.
- 4.10.21.7.1
(03-23-2023)
Treaty Benefit Criteria
- (1) To claim treaty benefits with respect to U.S. source FDAP income, a foreign person receiving a U.S. sourced payment must not only be a resident of the treaty partner country but must also derive and beneficially own the item of income for which the treaty benefits are claimed. In addition, the person must satisfy the requirements of the limitation on benefits (LOB) article, if any, contained in the treaty, as well as any other specific treaty requirements contained in the treaty for that item of income (See Treas. Reg. 1.1441-6 for more information on the foreign person's documentation requirements to claim treaty benefits at source.)
- (2) A foreign taxpayer that is claiming treaty benefits for an item of income for which Chapter 3 would otherwise impose a 30 percent withholding obligation, must certify under penalties of perjury that it has satisfied the applicable requirements under the relevant income tax treaty (see Form W-8BEN-E Part III - Claim of Treaty Benefits). The following requirements are applicable to foreign persons that are claiming treaty benefits. These requirements are also briefly explained separately in the following subsections:
- a. Resident of treaty country
 - b. Beneficial owner of the income

- c. “Derived by” (in discussion of fiscally transparent entities, hybrid entities and reverse hybrid entities)
- d. Limitation on benefits

4.10.21.7.1.1
(03-23-2023)
**Resident of Treaty
Country**

- (1) A foreign person that is claiming benefits under an income tax treaty must be a resident of the relevant treaty country. The 2016 U.S. Model Treaty, Article 4, defines “resident of a Contracting State” as any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, citizenship, place of management, place of incorporation, or any other criterion of a similar nature. A resident of a Contracting State includes that State and any political subdivision or local authority thereof. It also provides that a person who is liable to tax in respect only of income from sources in a Contracting State or of profits attributable to a permanent establishment in that State is not a resident of that State.
- (2) A nonresident noncitizen individual who is claiming benefits under an income tax treaty must be liable to tax in that country as a tax resident. This is a determination made under foreign law whose treaty is being applied, often based on the individual’s days of physical presence in that country.
- (3) An individual may be a resident under the laws of the United States and a treaty country (dual resident individual). This happens frequently in the case of U.S. green card holders who are living in a treaty country. A dual resident must apply the treaty tie-breaker rule (generally in Article 4 (Residence) of the treaty) to see if he or she may claim treaty benefits with respect to income sourced in the United States. If the individual applies a series of tests and determines that he or she is solely a resident of the treaty country, the individual may file a Form W-8BEN or a Form 8233 to claim treaty benefits. The individual must also comply with the reporting requirements in Treas. Reg. 301.7701(b)-7.

4.10.21.7.1.2
(09-20-2018)
Beneficial Owner

- (1) The foreign person must also be the beneficial owner of the item of income for which it is claiming treaty benefits. Treas. Reg. 1.1441-1 (c)(6) defines the term beneficial owner for withholding tax purposes, **but not for purposes of claiming a benefit under an income tax treaty**. Treaties generally do not define the term “beneficial owner” but the technical explanations to treaties often state that the term is defined under the internal law of the country imposing tax (i.e., the source country). In other words, the beneficial owner of dividend, interest, royalty income, or other income under Articles 10, 11, 12 and 21, respectively of the Model Treaty, as the case may be, cannot be a nominee, agent, or custodian of the payment for U.S. tax purposes. See, e.g., *Aiken Industries v. CIR*, 56 T.C. 925, 933 (1971).
- (2) In addition, the conduit regulations under IRC 7701(l) and Treas. Reg. 1.881-3 apply to determine the beneficial owner, as do judicial principles such as substance over form and step transaction doctrine, assignment of income, and constructive ownership. See, e.g. *Del Commercial Properties, Inc. v. CIR*, T.C. Memo 1999-411, aff. 251 F.3d 210 (D.C. Cir. 2001); Treas. Reg. 1.1441-7(f)(2) discusses knowledge and reason to know standard concerning conduits.
- (3) Because the special rules in Treas. Reg. 1.1441-1(c)(6)(ii) do not apply, a partnership or disregarded entity that is a resident of a treaty country is not disqualified per se from being the beneficial owner of an item of income for treaty purposes. It may beneficially own an item of income as long as it is a

treaty resident that derives the item of income, and, taking into account all the facts and circumstances, it is not acting as an agent or nominee or conduit of another person.

4.10.21.7.1.3
(09-20-2018)
**“Derived By” (See IRC
894 and Treas. Reg.
1.894-1(d))**

- (1) An item of U.S. sourced FDAP income paid to a foreign entity is not eligible for treaty benefits unless the income is “derived by” a resident of a treaty jurisdiction under Treas. Reg. 1.894-1(d). An item of income may be derived by the entity receiving the item of income, by the interest holders (e.g., partners, members, or other unit holders) of the entity that receives the income or, in certain circumstances, both (dual treaty claims are explained in paragraph (7) below).
- (2) An item of income paid to an entity shall be “derived by the entity” only if the entity is not fiscally transparent under the laws of the entity’s jurisdiction with respect to the item of income. See Treas. Reg. 1.894-1(d)(1) and (d)(3)(ii).
- (3) An item of income paid to an entity is “derived by its interest holder (not the entity)” only if under the laws of the interest holder’s jurisdiction: (1) the interest holder itself is not fiscally transparent with respect to the item of income, and (2) the entity receiving the payment is fiscally transparent under the laws of the interest holder’s jurisdiction with respect to the item of income. See Treas. Reg. 1.894-1(d)(1) and (3)(iii).
- (4) To the extent that, under the laws of the country in which the fiscally transparent entity (FTE) is a resident, of the income flows through the FTE to its owners, the income is not derived by the entity and the entity is thus ineligible for a reduced withholding tax rate under the treaty. However, a treaty-reduced withholding rate may apply at the interest holder level depending on the status of the interest holders (and whether such persons meet all the requirements of the treaty). The focus is on the law of the applicable foreign jurisdiction or jurisdictions, and not whether the entity is fiscally transparent for U.S. tax purposes.
- (5) Notwithstanding the preceding provisions, an item of income paid directly to a type of entity specifically identified in a treaty as a resident of a treaty jurisdiction shall be treated as derived by a resident of that treaty jurisdiction. See Treas. Reg. 1.894-1(d)(1).
- (6) To more fully understand the concept of “derived by” it will be helpful to briefly describe fiscally transparent entities, hybrid entities and reverse hybrid entities below. The related topic of limitation of benefits is discussed after “derived by”, fiscally transparent entities, hybrids and reverse hybrids.
- (7) A dual treaty claim occurs when a foreign entity and its interest owners are both claiming treaty benefits for an item of income, either each claiming separate portions of the same item of income, or both claiming the same portion of the income. The withholding agent may, at its option, accept such dual claims based on withholding certificates or other appropriate documentation furnished by the entity and its interest holders, or reject both claims. See Treas. Reg. 1.1441-6(b)(2)(iii) and (iv) for more information. If a foreign entity is not fiscally transparent in its own jurisdiction, it may claim a reduced rate of tax under a treaty as the beneficial owner of any portion of income to the extent the entity is receiving income by providing valid Form W-8BEN-E to the withholding agent; If a foreign entity is treated as fiscally transparent in any interest holder’s jurisdiction, it acts as a flow-through entity claiming a reduced

rate of tax on behalf of any of its interest holders with respect to the same or a different portion of the income by providing the withholding agent a Form W-8IMY and other supporting documentation (e.g., interest holder's Form W-8BEN or W-8BEN-E, and withholding statements).

4.10.21.7.1.3.1
(09-20-2018)

**Fiscally Transparent
Entities (FTEs)**

- (1) Treas. Reg. 1.894-1(d) applies to any entity if it is FTE either in the United States, its country or organization or the country in which its interest holders are resident. It doesn't have to be FTE in all countries. A general partnership is an example of an entity that is typically treated as an FTE under the laws of the United States and its treaty partners, although it is important to note that some treaty partners do not have the concept of a FTE at all under their domestic law. In contrast, a limited liability company is typically not treated as fiscally transparent by most of our treaty partners, with some specific exceptions. Rather it is taxed at the entity level as a company. Treas. Reg. 1.1441-1(c) (23) defines a flow-through entity as any entity, such as a foreign partnership (not a withholding partnership), that may provide documentation on behalf of its partners, beneficiaries, or owners to a withholding agent.
- (2) An entity is fiscally transparent for treaty purposes if the income received by the entity is currently includable in the income of its interest holders under the laws of their respective countries of residence (e.g., the entity's partners, members, or other unit holders), whether or not distributed by the entity, and the income retains its character and source in the hands of the interest holder (see Treas. Reg. 1.894-(d)(3)(ii) (under law of entity's jurisdiction) and (iii) (under law of interest holder's jurisdiction). Conversely, an entity is not fiscally transparent if the income received by the entity is treated as not currently includible in the income of its interest holders. There is no requirement under Treas. Reg. 1.894-1(d)(3)(ii) that the character of the income remain the same as in the United States if the foreign entity is not fiscally transparent.
- (3) The determination of whether an entity is a FTE is made on an item-by-item basis and documentation (e.g. Forms W-8) is key. See Treas. Regs. 1.894-1(d) and 1.1441-6(b)(2).
- (4) The exam team should determine if the withholding agent properly performed Chapter 3 withholding responsibilities in part by requesting, validating, and reasonably relying upon proper withholding certifications.
- (5) If an entity is fiscally transparent under the laws of the entity's jurisdiction with respect to an income item, and its interest holders can claim treaty benefits with respect to such income, the entity should provide the withholding agent a Form W-8IMY as an intermediary.

4.10.21.7.1.3.2
(09-20-2018)

Hybrid Entity

- (1) For treaty purposes, a hybrid entity is an entity that is treated as fiscally transparent in one jurisdiction, but not the other. A domestic hybrid entity is a U.S. entity that is fiscally transparent for U.S. tax purposes, but not fiscally transparent for foreign tax purposes.
- (2) A foreign hybrid entity is a foreign entity that is fiscally transparent for U.S. tax purposes, but not fiscally transparent for foreign tax purposes. Withholding agents should be able to identify hybrid entities because they should be properly identified as such in Part I, Line 4 of the Form W-8BEN-E (such as a partnership). Hybrid entity status is relevant for claiming treaty benefits. A hybrid entity is required to provide its Chapter 4 status if it is receiving a withholdable payment.

- 4.10.21.7.1.3.3
(09-20-2018)
Domestic Reverse Hybrid
- (1) According to Treas. Reg. 1.894-1(d)(2), a domestic reverse hybrid (DRH) entity is a U.S. entity that is not treated as fiscally transparent for U.S. tax purposes, but is treated as fiscally transparent for foreign tax purposes under the laws of the interest holder's jurisdiction, with respect to the item of income received by the domestic entity.
 - (2) An income tax treaty may not apply to reduce the amount of federal income tax on U.S. source payments received by a domestic reverse hybrid entity because the payment is made to a domestic corporation and not to a foreign person for withholding purposes. Foreign interest holders in a DRH may claim reduced withholding on payments made by the DRH to them if correct documentation is provided, even if the interest holder does not take into account the payment by a DRH because it is treated only as a partnership distribution. Certain important exceptions apply in the case of deductible payments made by a DRH to its related interest holders. See Treas. Reg. 1.894-1(d)(2)(ii)(B).
- 4.10.21.7.1.3.4
(09-20-2018)
Foreign Reverse Hybrid
- (1) A foreign reverse hybrid entity is a foreign entity that is treated as not fiscally transparent for U.S. tax purposes, but it is fiscally transparent for foreign tax purposes.
- 4.10.21.7.1.4
(03-23-2023)
Limitation of Benefits (LOB)
- (1) The Limitation on Benefits (LOB) article is an anti-treaty shopping provision included in many U.S. income tax treaties. The purpose of the LOB provisions is to deny treaty benefits to taxpayers that have only a minimal nexus to the treaty country, e.g., when a resident of a non-treaty jurisdiction establishes an entity in a treaty jurisdiction solely to access the benefits of a treaty. The LOB rules help prevent this by generally requiring the taxpayer to satisfy at least one of the objective tests contained in the LOB article to be eligible for treaty benefits (See IRM 4.60.2.7.1 Limitation on Benefits (LOB) Requirement).
- 4.10.21.7.1.4.1
(03-23-2023)
LOB and LOB Standards
- (1) Most treaties have a LOB provision, which an entity resident in a treaty country must satisfy to obtain benefits under that country's tax treaty with the United States. Among other things, this provision is intended to prevent residents of a non-treaty country or of a treaty country with less favorable benefits from inappropriately accessing benefits under that particular tax treaty. The LOB provisions generally require the taxpayer seeking treaty benefits to satisfy at least one of the objective tests or safe harbors (IRM 4.60.2.7.1 Limitation on Benefits (LOB) Requirement), or obtain discretionary relief from the U.S. Competent Authority (CA) (IRM 4.60.3.2.22 and 4.60.3.2.23).
 - (2) Common objectives tests include: ownership and base erosion test, publicly traded company or subsidiary of a public company test, base erosion test, active trade or business test, derivative benefits test (which is generally limited to treaty partners that are members of the EU, NAFTA, the EEA, and Switzerland). For brief summary of above tests, see pp. 11 of the 2021 W-8 BEN-E Instructions.
 - (3) A withholding agent may rely on the beneficial owner's claim that it meets the LOB provision specifically identified on the Form W-8BEN-E, absent actual knowledge that such claim is unreliable or incorrect. See Treas. Reg. 1.1441-6(b)(1)(i).
 - (4) In cases where documentary evidence is provided in lieu of Form W-8BEN-E, Treas. Reg. 1.1441-6(c)(5)(i) requires a treaty statement that expressly provides

that the foreign taxpayer meets a treaty LOB provision and specifically identifies the LOB provision(s) relied upon in the applicable tax treaty.

- (5) As indicated above, Treas. Reg. 1.1441-6(b)(1)(ii) specifically includes as part of the reason to know standard the existence of an applicable treaty.
- (6) During a Form 1042 exam, the revenue agent generally need not require the withholding agent to obtain an attachment to the Form W-8BEN-E, describing the beneficial owner's analysis of how it met the LOB provisions relied upon (as the regulations do not require withholding agents to do this).

4.10.21.7.1.4.2
(03-23-2023)
**LOB Form W-8 BEN-E
Checkboxes**

- (1) Effective with the April 2016 revision of Form W-8BEN-E, new checkboxes have been added to the Form W-8BEN-E's Part III (Claim of Tax Treaty Benefits) for each of the common objective tests that must be met by a taxpayer to satisfy an applicable treaty's LOB provision to claim treaty benefits. There is also a new box to check if the foreign entity providing the form obtained a favorable discretionary determination from the U.S. competent authority (see instructions for Form W-8BEN-E). The Form 1042-S (F1042-S) has a new box to list the LOB code corresponding to a LOB checkbox on the W-8BEN-E (see Form W-8BEN-E and Exhibit 4.10.21-6). Note that withholding agents are generally expected to report LOB codes on Form 1042-S beginning in 2018.

4.10.21.7.1.4.3
(03-23-2023)
**Discretionary
Determinations by
Competent Authority**

- (1) The discretionary determinations referred to in IRM 4.60.2.7 and in Part III of the Form W-8BEN-E relate to U.S. competent authority determinations granting treaty benefits to a foreign entity despite the entity's failure to meet one of the objective tests provided in the LOB article of the applicable treaty. While not required, the revenue agent may, as a best practice, contact the U.S. competent authority to obtain a copy of the discretionary determination when there is a treaty claim and the documentation related to such claim indicates that the entity has obtained a favorable discretionary determination from the U.S. competent authority (e.g., taxpayer checks the box for "Favorable discretionary determination by the U.S. competent authority received" on Form W-8BEN-E, Part II, Line 14(b)). If the revenue agent finds that such determination from U.S. competent authority does not exist, it may, subject to the limitations under IRC 6103, notify the withholding agent that such claim of reduced rate pursuant to an income tax treaty is incorrect and as such should not be relied upon going forward. Note that a withholding agent that receives notification from the IRS that a claim of U.S. status or a reduced rate is incorrect will have actual knowledge that such claim is incorrect beginning on the date that is 30 calendar days after the date the notification is received. See Treas. Reg. 1.1441-1(e)(1)(ii)(B) and 1.1441-7(b)(1). See Rev. Proc. 2015-40, IRM 4.60.3.2.3 for further details on examiner procedures concerning discretionary determinations.

4.10.21.7.1.4.4
(03-23-2023)
LOB Cross-Reference

- (1) For a general background discussion of Limitation of Benefits, see:
 - IRM 4.60.2.7.1 – Limitation on Benefits (LOB) Requirement
 - IRM 4.60.3.2.22 -Discretionary Limitation on Benefits (LOB) Requests
 - IRM 4.60.3.2.23 – U.S. Competent Authority's Role in LOB Requests
 - Exhibit 4.60.3-1 – Terms/Definitions/Acronyms – LOB

4.10.21.7.2
(03-23-2023)

Withholding Agent Due Diligence Standards with Respect to Treaty Benefits Claimed by Foreign Entities

- (1) This IRM now turns to a discussion of the standards to which withholding agents must adhere to in determining the proper Chapter 3 withholding tax rate to apply on U.S. sourced FDAP income paid to foreign persons, specifically when applying a reduced rate of withholding pursuant to a treaty claim made by a foreign entity. Revenue agents will want to verify during the course of a Form 1042 exam that withholding agents are properly applying these standards.
- (2) During a Form 1042 examination, where U.S. sourced FDAP income is subject to Chapter 3 withholding but treaty benefits are being claimed, revenue agents should determine whether the withholding agent properly reduced the withholding tax rate based upon the foreign taxpayer's representation that it met the criteria necessary to be entitled to treaty benefits and the rate of tax that applies under the treaty. The revenue agent should verify that the withholding agent followed the due diligence standards contained in Treas. Reg. 1.1441-7(b) in determining the correct withholding and reporting. This is generally done by verifying that the withholding agent reasonably relied (see IRM 4.10.21.9.4) on the appropriate, complete, and timely provided a withholding certificate such as a Form W-8BEN-E (or documentary evidence if applicable) (See IRM 4.10.21.6). According to Treas. Reg. 1.1441-1(e)(4)(viii), a withholding agent may rely on the information and certifications stated on withholding certificates or other documentation without having to inquire into the veracity of this information or certification, unless it has **actual knowledge or reason to know** that the information or certification is incorrect. However, a withholding agent has reason to know that a beneficial owner's claim of treaty benefits is incorrect or unreliable if such Form W-8BEN-E includes a claim for treaty benefits, but there is no U.S. income tax treaty in force with the recipient's country of residence during the year of payment (See Treas. Reg. 1.1441-6(b)(1)(ii)).
- (3) For purposes of Chapter 3, if a withholding agent has reason to know (IRM 4.10.21.9.3) or has actual knowledge (IRM 4.10.21.9.3.2) that a Form W-8BEN-E, or alternative documentation (in the case of payments with respect to offshore obligations) is incorrect or unreliable, then the withholding agent must withhold, deposit, and report at the 30% IRC 871(a), IRC 881(a), IRC 1441(a) and IRC 1442(a) rate; otherwise, a withholding agent could be liable for tax, interest, and penalties to the extent provided under IRC 1461 and IRC 1463 and the regulations thereunder. If withholding is applied under Chapter 4, no withholding is required under Chapter 3. In addition to a Form 1042 examination, the revenue agent and the Form 1042 exam team manager should consider making a referral to Cross Border Activity Practice Area to open a Form 1120F exam for any balance due, and any other underpayments for which a Form 1120F filer may be liable.

4.10.21.7.3
(09-20-2018)

Form 8833 – Treaty-Based Return Position Disclosure Under IRC 6114 or 7701(b)

- (1) Form 8833 is used by taxpayers to make the treaty-based return position disclosures required by IRC 6114 and the regulations thereunder. A treaty-based return position is a claim that the provision of a treaty modifies or overrules an IRC provision and thereby cause or potentially cause a reduction of tax on the taxpayer's U.S. income tax return. Reporting is required under Treas. Reg. 301.6114-1(b), except as expressly waived under Treas. Reg. 301.6114-1(c). The following list is not a list of all positions for which reporting is required under this section but is a list of some of the most common positions for which reporting is specifically required.

- a. That a nondiscrimination provision of a treaty precludes the application of any otherwise applicable Code provision, other than with respect to the making of or the effect of an election under IRC 897(i)
 - b. That a treaty reduces or modifies the taxation of gain or loss from the disposition of a United States real property interest
 - c. That a treaty exempts a foreign corporation from tax because the foreign corporation does not have a permanent establishment in the United States;
 - d. That a treaty reduces the amount of tax with respect to the branch profits tax (IRC 884(a)) or the tax on excess interest (IRC 884(f)(1)(B));
 - e. That a treaty resources an amount of income that would otherwise be U.S. source as foreign source.
- (2) There may be occasions when a revenue agent will be conducting a Form 1042 examination related to an ongoing or potential Form 1120, 1120F, 1040NR or other examination. In such cases, the revenue agent may wish to inspect any Form 8833 attached to the relevant return. The Form 1042 examiner could request a copy of Form 8833 through collaboration with the Form 1120, 1120F, 1040NR, or another exam team, as the case may be. The Form 1042 revenue agent might also request Form 8833 from the taxpayer via an IDR, stipulating it is for inspection purposes. Another way for the Form 1042 revenue agent to obtain a copy of the Form 8833 is through the EUP system and/or LIN Link. The Form 8833 may provide further explanation to the characterization of the income and nature of the treaty benefits relied upon, adding to the revenue agent's total understanding of the facts and circumstances, and may be used to verify consistency with the withholding certificate's treaty claims in the Form 1042 exam.
- (3) Where U.S. sourced FDAP income has been properly reported on Form 1042-S, the filing of Form 8833 is generally not required.
- (4) However, there are times the Form 8833 may be required for FDAP payments.
- Example:** Reporting on a Form 8833 is required for a foreign corporation (beneficial owner) that receives more than \$500,000 in U.S. sourced FDAP income (Treas. Reg. 1.1441-2(a)) from a related payer, and the foreign corporation is claiming reduced withholding under a treaty with a LOB provision. See Treas. Reg. 301.6114-1(b)(4)(ii)(C).
- (5) See Treas. Reg. 301.6114-1(b) and (c) and Form 8833 instructions for guidance when the Form 8833 reporting is specifically required or the reporting requirement is waived, as the case may be.
- (6) Failure to disclose any of these positions on a Form 8833 will result only in the imposition of penalties on the person that has failed to disclose the position as provided in IRC 6712, and not in the denial of the claimed treaty benefit by the taxpayer, provided it can ultimately establish its entitlement to the benefit.

4.10.21.8
(03-23-2023)
**Important Items to
Consider in Preparing
for a Form 1042 Audit**

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- c. Does each beneficial owner/recipient have an electronic folder in which all relevant documents are maintained?
 - d. Does the taxpayer maintain an electronic W-8 system? If so, the examiner should request that the taxpayer provide a description.
 - e. Did the taxpayer ever enter a memorandum of understanding (MOU) with IRS regarding an electronic W-8 system? If so, the examiner should request a copy of the MOU.
 - f. If the taxpayer entered an electronic W-8 MOU but is not following the MOU, the examiner should request the taxpayer to explain why.
- (4) An audit of Form 1042 may result in an adjustment to both Form 1042 and Form 945 (for backup withholding that may apply under the presumption rules). Therefore, when auditing Form 1042, the examiner must always determine the statute of limitations on the audit years for both Form 1042 and Form 945. If applicable, the examiner is required to obtain and have executed Form 872 and Form SS-10 to protect the statute of limitations for Form 1042 and Form 945, respectively. See IRM 25.6.22 and Pub 1035 for more details.
- (5) It is highly recommended that the examiner determines whether the taxpayer has entered into any agreements with the IRS regarding their withholding systems, policies, procedures or other requirements, such as a:
- a. Closing agreement
 - b. Pre-filing agreement for the audit year
 - c. Memorandum of understanding (including one covering an on-line Form W-8 system)
- If so, examiner should obtain a copy of the memorandum, agreement or submission for background and to ensure that the taxpayer has satisfied any of its conditions applicable to the audit year.
- (6) An examiner should determine whether a withholding agent submitted delinquent returns under withholding agent disclosure procedures for a prior tax year (see IRM 4.10.21.8.1). If so, review a copy of the withholding agent's reasonable cause penalty waiver request memo and any corrective procedures described to verify they are in place during the audit year.
- (7) Examiners should always be aware that a withholding agent and a beneficial owner (typically the "payee") are separate taxpayers and that the disclosure rules under IRC 6103 apply.

4.10.21.8.1
(03-23-2023)
**Procedures for
Accepting Delinquent
Withholding Tax Returns
in Connection with
Withholding Agent
Voluntary Disclosure**

- (1) When returns are received under these procedures, FPP revenue agents will review the information submitted and consider a request for penalty relief if one is included. Each submission may be subject to an audit referral, with approval by the FPP territory manager. These procedures do not provide determinations by the IRS about whether a payment (such as the amount, timing, character, or source of such payment) was subject to withholding.

4.10.21.8.1.1
(08-29-2019)
**Requirements for Using
These Procedures**

- (1) To use these procedures, a withholding agent must submit any delinquent withholding tax returns, including related information returns, along with full payment of the tax due and a statement including:

- a. An explanation of the areas or lines of business for which there was non-compliance with tax, withholding and reporting obligations on payments to foreign persons
 - b. An explanation of how the non-compliance was discovered
 - c. A description of corrective procedures implemented to ensure future compliance
 - d. A copy of the procedures described in item (c) as communicated to employees or other responsible parties of the withholding agent
 - e. The withholding agent cannot have filed delinquent returns using these procedures in prior years.
- (2) A withholding agent may file delinquent returns using these procedures if it is a withholding agent, as defined in Treas. Reg. 1.1441-7(a)(1) of the Income Tax Regulations, that is not a qualified intermediary, a withholding foreign partnership, or a withholding foreign trust,, as these entities are subject to other agreements.
 - (3) The withholding agent must report and remit any tax not already paid and will be expected to pay interest and any penalties for which relief is not otherwise granted pursuant to these procedures. In cases involving large underpayments, the IRS will consider the withholding agent's proposal for payment of the liability in more than one installment or will consider the withholding agent's posting of a cash bond under the procedures outlined in Rev. Proc. 2005-18, 2005-1 C.B. 798.
 - (4) The IRS reserves the right to verify that corrections to the withholding agents' procedures have been made. This verification does not constitute an examination. If the IRS determines an examination is warranted the withholding agent will be notified and the examination will be completed as soon as possible.
 - (5) The IRS will issue an acknowledgment letter at the conclusion of its verification, if the IRS is satisfied that the withholding agent has corrected its systems and has paid or made satisfactory arrangements to pay the outstanding liabilities that arose from the delinquent return filings.

4.10.21.8.1.2
(08-29-2019)
**Withholding Agents
Currently Under
Examination**

- (1) A withholding agent is not eligible to use these procedures if the withholding agent is under examination with respect to any liabilities related to withholding tax filings on the date of the delinquent return(s) submission. For this purpose, an examination is treated as commencing on the date the withholding agent receives notification from the IRS of an impending examination or of an impending referral for examination. In addition, filing under these procedures is not available to any withholding agent that has the same issue pending in Appeals or is in litigation on issues involving Chapter 3 or 4 tax, withholding, or reporting obligations.

4.10.21.8.1.3
(03-23-2023)
Enforcement Period

- (1) Consistent with IRM 1.2.1.6.18, the filing of delinquent returns generally applies to six (6) years of non-filed/delinquent returns with managerial approval required for any additional years.

4.10.21.8.1.4
(08-29-2019)
No Closing Agreement

- (1) The IRS will not provide a closing agreement for any submission. The delinquent returns received will be processed in accordance with IRM 4.4.9, Delinquent and SFR Processing.

4.10.21.8.1.5
(08-29-2019)

**Requests for Penalty
Relief Under Reasonable
Cause**

- (1) For penalty relief to be considered, the withholding agent must provide a request for penalty relief and include, at a minimum, the following items with their submission package:
- a. A description of the current procedures the withholding agent uses to determine tax, withholding, and reporting obligations regarding payments to foreign persons, as previously mentioned.
 - b. A description of the failures in the withholding agent's tax, withholding, and reporting procedures for payments to foreign persons, why the failures occurred, and the years affected by such failures, as previously mentioned.
 - c. The number of persons affected by such failures and how the number was determined.
 - d. A calculation of the total amount of taxes the withholding agent failed to withhold, pay, or report, not including interest and penalties, for tax periods open for assessment or collection under the provisions of IRC 6501. This calculation should identify any adjustments under IRC 1463 for tax already paid and provide documentation of the same.
 - e. A list of the documents being provided with the submission.
 - f. A required penalties of perjury statement: The following declaration must accompany a submission, any information submitted after the original submission, or any subsequent change in the submission. "Under penalties of perjury, I declare that I have examined this submission, including the accompanying documents listed below, and to the best of my knowledge and belief the facts presented in support of this request are true, correct, and complete. "
 - g. The declaration must be signed by the withholding agent, not the withholding agent's representative, as stated under Treas. Reg. 301.6651-1 (c).

4.10.21.8.1.6
(03-23-2023)

**Required Related
Information**

- (1) In addition to the information described above the delinquent return filing must contain the following:
- a. The related information return Forms 1042-S with signed Form 1042-T if filing on paper, or a schedule of them if filed electronically.
 - b. Information returns on Form 1042-S must indicate the withholding tax was paid by the withholding agent unless the withholding agent actually withheld the tax at the time the payment was made to the recipient.
 - c. Include a spreadsheet tying the information returns to the primary Form 1042 if there are more than 25 information returns.
 - d. A properly completed Form 2848, if applicable. To appear before the IRS regarding the submission, a representative must comply with the requirements of IRM 4.11.55.2.6.

4.10.21.8.1.7
(03-23-2023)

**Submissions under
Voluntary Disclosure
Procedures**

- (1) Send the signed, original delinquent tax returns, payment, and related information to:
- Internal Revenue Service
Attn: WEIIC, W&C Team 1743
5100 River Road, MS 603
Schiller Park, IL 60176-1076

- (2) Questions or messages relating to these procedures may be left at (630) 493-5009. Calls will normally be returned within 5 business days.

4.10.21.9
(09-20-2018)

**U.S. Financial Institution
Withholding Agent Audit**

- (1) Commercial banks and brokerage firms are examples of financial institutions that act as U.S. withholding agents. Certain of these institutions act as intermediaries with respect to their clients' investments in securities and deposits. As a result, these institutions may make investments and receive payments in a fiduciary or custodial relationship with their clients. For example, when a foreign person's account is credited by a broker-dealer with U.S. source FDAP income that the broker-dealer has received on the foreign person's behalf, the financial institution may have reporting and withholding responsibilities with respect to the income. This type of audit will focus on determining if such amounts paid to account holders have been properly subjected to Chapter 3 and Chapter 4 withholding and reporting, including whether any payments treated as paid to foreign persons should have instead been subjected to backup withholding under IRC 3406.
- (2) A financial institution can have many business lines that create payments subject to Chapter 3 and Chapter 4 reporting and withholding, such as custodial or depository businesses. An examiner should look for names such as investment or custodial services, asset management, retiree or pension fund administration, wealth management, lines of credit, prime brokerage, and depository. Financial institutions have a variety of client bases, including both direct and indirect clients. Some financial intermediaries may deal primarily with institutional clients, while a retail bank may have large numbers of individual account holders. It is important to understand the taxpayer's business model to better tailor the audit and capture the entire payee population. For example, some institutions document account holders at each line of business whereas others maintain a universal account system. Also note that financial institutions often make payments to foreign persons (outside of their financial institution function) that can be subject to reporting and withholding (see IRM 4.10.21.10.3).
- (3) Due to the volume of payments processed by financial institutions, it is important that examiners analyze the withholding tax system and internal controls relating to the withholding process. The examiner should determine if the taxpayer has entered into any agreements with the IRS (i.e., MOUs, prior closing agreements) that would affect withholding procedures. Typically, payee status is determined upon account opening, often performed by an employee of the withholding agent, such as an account manager. A review of the withholding certificate, or documentation validation, is often centralized. Account opening information is transcribed into an account opening system along with Know Your Customer (KYC) information, which is ultimately fed into a comprehensive account master file. Hard copies of documents may be scanned into these systems for easy retrieval.
- (4) Tax and tax documentation information (such as for Forms W-8) are fed into a tax reporting system for validation purposes. This may occur daily for large institutions. This system will ultimately populate the information on Form 1042 and Form 1042-S. Withholding agents may have a separate custodial account system that records receipts and payments daily.
- (5) Examiners should ask for an explanation (or copies) of the withholding and reporting procedures and if separate procedures apply for each line of business. Some financial instruments may produce payments where the

income type classification is unclear, which can affect reporting, treaty rates, or exemptions from withholding. Internal systems will often flag uncertain payment types and prompt an employee to consult the underlying source documents or look to third-party providers that provide source and income information

4.10.21.9.1
(09-20-2018)
**Functional Review of
Operational Procedures**

- (1) The examiner should perform a functional review of the U.S. withholding agent's withholding tax related operating procedures for capturing and validating payments subject to withholding and client related information relevant to withholding or reporting.

4.10.21.9.1.1
(09-20-2018)
**Review of Written
Procedure and Training
Manuals**

- (1) The first step is a review of written procedure and training manuals such as:
- Summaries of withholding tax systems
 - System flow charts covering payments made to account holders
 - Internal control, audit reports or other information which relate to the withholding tax function
 - Payment system design manuals
 - Account opening procedure manuals
 - Validation procedures for Form W-8
 - Procedures for determining or classifying undocumented accounts;
 - Deposit procedures
 - Procedures to apply the reimbursement/set-off procedures (if applicable)
 - Procedures to apply escrow procedures (if applicable)
 - Application of presumption rules to undocumented accounts
 - Other manuals related to functions that may have withholding tax implications

Evaluation of the above written procedures (or lack thereof) may provide the examiner with an indicator of the overall reliability of the taxpayer's withholding tax functions. This assessment may assist in determining the extent of additional audit procedures, such as the review of account files statements and withholding certificates.

4.10.21.9.1.2
(09-20-2018)
Review of Form 1042

- (1) **Reconciliation:** The gross income, net tax liability and withholding reported on Form 1042 should generally match the gross income and taxes withheld as determined by combining these amounts from all Forms 1042-S filed. To verify this, the examiner should obtain the taxpayer's reconciliation workpapers and Forms 1042-S and should compare Form 1042 with aggregate amounts from Forms 1042-S. The examiner can also request for a computer audit specialist (CAS) to perform a reconciliation in certain cases of payments and Forms 1042-S contained in computer sensitive files.

Note: Examiner should account for line 67 (former line 66) of Form 1042, Credit for amounts withheld by other withholding agents, during the reconciliation process and should ensure that the credit is supported by Forms 1042-S issued to the withholding agent.

- (2) **Deposit Requirements:** The tax liability for each applicable period of the year (normally quarter-monthly which is the 7th, 15th, 22nd and last day of the month) is required to be shown in the Record of Federal Tax Liability section on Form 1042. The examiner should ensure that the withholding agent did not instead complete this section, in some situations, based on deposit dates, as this error may prevent identification of late deposits. The examiner should

otherwise ensure that deposits were made timely by reviewing the taxpayer's payments and deposits records. Due dates for deposits and associated penalties are discussed below:

- If the total withholding tax for a calendar year is less than \$200, the tax can be paid when the tax return (Form 1042) is timely filed.
- If at the end of any calendar month the total amount of withholding tax is more than \$200 but less than \$2,000, the withholding agent must deposit the taxes within fifteen days after the end of the month.
- If at the end of any quarter-month period the withholding tax is \$2,000 or more, the withholding agent must deposit taxes within three banking days after the end of the quarter-monthly period.

- (3) **Escrow Procedures:** If the withholding agent applied escrow procedures under Treas. Reg. 1.1441-3(d) (e.g., determined by a review of Forms 1042-S or through a review of the withholding agent's coding for withholding purposes), the examiner should also look at the Form 1042 filed for the previous year or any filed in the subsequent year to ensure that the reporting of withholding under these procedures was done correctly. The corollary rule for Chapter 4 can be found in Treas. Reg. 1.1471-2(a)(5)(ii).
- a. Under the escrow procedures, if a withholding agent cannot determine the source of the income or the amount that is subject to withholding, it can withhold at the maximum rate of 30% but instead of depositing such amount withheld, it can elect to hold that 30% in escrow until the earlier of the date that the determination of the amount subject to withholding is made or one year from the date that the amount is placed in escrow at which time the withholding becomes due. To the extent that withholding is not required, the escrowed amount must be repaid to the payee.
 - b. If the escrow procedures are followed, a Form 1042 for a calendar year may include the income that was paid to all recipients during the calendar year but if escrow procedures were followed, the form will not include the tax withheld as part of the tax withheld or tax liability. Instead, such amounts will be reported as tax withheld and as part of the tax liability in the Form 1042 for the following year. See Instructions to Form 1042 for reporting requirements when applying escrow procedures.
- (4) **Adjustments for overwithholding:** Examiners should also review whether the withholding agent applied the reimbursement or set-off procedures under Treas. Reg. 1.1461-2, and if so, whether the application of such procedures was properly applied and reported on Forms 1042 and should compare to Forms 1042-S. See Instructions for Form 1042 and Instructions for Form 1042-S for additional guidance on how to account for adjustments for overwithholding on Forms 1042 and 1042-S.

4.10.21.9.1.3
(09-20-2018)

Review of Form 1042-S

- (1) With the assistance of the CAS, year-end account statements (or the information included on them) should be obtained on a sample basis. The Forms 1042-S for these accounts should be compared to verify the correctness of such items as:
- Gross income (Box 2)
 - Tax Withheld (Box 7)
 - Income code (Box 1)
 - Tax rate (Box 3b or 4b)
 - Exemption code (Box 3a or 4a)

- Recipient status code (Boxes 13f and 13g)
- Recipient's account number (Box 13k) (for an account for which a foreign TIN, or reasonable explanation for the absence of, is required (see Notice 2017-46))

- (2) See Form 1042-S instructions for income, exemption and recipient codes, and other application form requirements. Tax treaty tables can be found at: <https://www.irs.gov/individuals/international-taxpayers/tax-treaty-tables>.

4.10.21.9.2
(09-20-2018)

**Account
Opening/Updating
Procedures**

- (1) Normally the status of an account holder, the withholding rates and other information are entered into the withholding agent's systems. Generally, this can be expected to occur when an account is opened. These procedures are critical in determining:
- a. The status of the account holder as a foreign or U.S. person
 - b. The type of account holder (i.e. as an individual or entity and the type of entity)
 - c. For foreign persons, the basis of any treaty claims (and otherwise the account holder's tax residence)
 - d. The withholding tax rate, if any
 - e. The Chapter 3 and 4 status of the respective account holders
 - f. The account holder's foreign TIN (for an account for which a foreign TIN, or reasonable explanation for the absence of, is required (see Notice 2017-46))
- (2) See IRM Exhibit 4.10.21-3, New Account Examination Procedures, for details.

4.10.21.9.3
(09-20-2018)

**Due Diligence - Standard
of Knowledge**

- (1) The examiner should ensure that the withholding agent has applied the due diligence standards set forth in Treas. Reg. 1.1441-7(b)(1) in its determination of the correct reporting and withholding to be applied. Under this regulation, if a withholding agent knows or has reason to know that a withholding certificate (e.g. Form W-8BEN) or documentary evidence provided by the payee is unreliable or incorrect, the withholding agent must generally either withhold at the maximum tax rate of 30% or withhold at the backup withholding rate (currently 24%), as determined based on the presumption rules. If a withholding agent relies on an agent to obtain documentation, the withholding agent is generally considered to know, or have reason to know, facts within the knowledge of its agent.
- (2) For the standards of knowledge that apply for Chapter 4 purposes, see Treas. Reg. 1.1471-3(e).

4.10.21.9.3.1
(03-23-2023)

Reason to Know

- (1) Generally, a withholding agent will be considered to have reason to know a claim of foreign status or for a treaty-based withholding rate to be incorrect or unreliable if the statements contained in the withholding certificate or in other information which the withholding agent has, would cause a reasonable person to question the claims made. However, a more specific reason to know standard applies with respect to payments by financial institutions for determining a payee's foreign status or entitlement to a claim for treaty benefits. See Treas. Reg. 1.1441-7(b)(3)(i) (limits on reason to know).

Note: The account file information is relevant information for an examiner to make any such determinations.

- 4.10.21.9.3.2
(09-20-2018)
Actual Knowledge
- (1) Despite representations made on an otherwise valid withholding certificate or the presumption rules, a withholding agent must withhold and report based on its actual knowledge of facts concerning the recipient when that knowledge results in a higher rate of withholding than would have otherwise applied. For example, if a withholding agent makes a payment to a U.S. person and the withholding agent has actual knowledge that the U.S. person is acting as an agent for a foreign person, the withholding agent must treat the payment as if it was made to a foreign payee. (This example does not apply when the U.S. person is a financial institution.)
- 4.10.21.9.3.3
(09-20-2018)
Application of Presumption Rules
- (1) For Chapter 3 purposes, if a withholding agent cannot reliably associate a payment with a valid withholding certificate (or documentary evidence, when permitted, that the withholding agent is permitted to rely upon under the reason to know or actual knowledge standards), the withholding agent must follow the presumption rules contained in Treas. Reg. 1.1441-1(b)(3) to determine the status of the payee for withholding and reporting purposes. The IRC 1441 presumption rules are summarized below.
- 4.10.21.9.3.3.1
(07-29-2008)
Classification (Type of Entity)
- (1) The withholding agent must generally presume that a payee is an individual, a trust, an estate, a corporation or one of the persons enumerated under Treas. Reg. 1.6049-4(c)(1)(ii)(A)(i) through Treas. Reg. 1.6049-4(c)(1)(ii)(Q), or a partnership by following the rules under Treas. Reg. 1.1441-1(b)(3)(ii).
- 4.10.21.9.3.3.2
(03-23-2023)
U.S. versus Foreign Status (or NPFFI status)
- (1) Generally, a payment that a withholding agent cannot reliably associate with valid documentation is presumed made to a U.S. person that is a nonexempt recipient for Form 1099 / backup withholding purposes per Treas. Reg. 1.1441-1(b)(3)(iii). However, an entity payee will be presumed to be a foreign person if the entity is an exempt recipient (such as a corporation) there are certain indicia of foreign status, and the payment is a withholdable payment. See Treas. Reg. 1.1441-1(b)(3)(iii)(A).
- (2) If a withholdable payment is made to an entity, the entity is treated as a non-participating foreign financial institution (NPFFI), and Chapter 4 withholding applies.
- (3) A payment is generally presumed made to a foreign payee when it is a payment subject to Chapter 3 withholding (or a withholdable payment made to an entity). See Treas. Reg. 1.1441-1(b)(3)(iii)(D) and Treas. Reg. 1.6049(d)(2) and (3).
- 4.10.21.9.3.3.3
(09-20-2018)
Foreign versus U.S. Status of Partnership
- (1) Indicia of foreign status is also relevant for determining the status of a partnership as U.S. or foreign for a payment other than a withholdable payment. See Treas. Reg. 1.1441-5(d) for more details on partnerships' presumption rules.
- (2) If it is presumed or known that a payee is a partnership, the withholding agent must determine the classification of the partnership as foreign or domestic. A partnership is presumed to be foreign when its EIN begins with "98", where the payer's communications with the partnership are mailed to an address in a foreign country, or where the payment is made outside the United States with respect to an offshore obligation. In all other circumstances, the payer may presume that the partnership is domestic (in which event no NRA withholding tax is applicable, however, backup withholding may be triggered). See Treas. Reg. 1.1441-5(d)(3) for more details.

- (3) If the partnership is presumed to be foreign, it is not the beneficial owner of the income paid to it and the presumption rule is applied because the payments are not properly allocated to the partners (with Forms W-8 or documentary evidence that may be relied upon). If the partnership is presumed to be domestic, it is treated as a U.S. nonexempt recipient for backup withholding / Form 1099 reporting purposes.

4.10.21.9.4
(09-20-2018)

**Reliance on Withholding
Certificate (Form W-8)**

- (1) A U.S. withholding agent may generally (subject to reason to know and actual knowledge standards) rely on a properly completed withholding certificate (i.e., Forms W-8), as defined in Treas. Reg. 1.1441-1(c)(16), to establish a recipient's foreign status or a claim of treaty benefit, special status for withholding purposes (such as a foreign tax-exempt organization), or Chapter 4 status (when a withholdable payment is made). Documentary evidence can instead be used with respect to offshore obligations as described in Treas. Reg. 1.6049-5(c).
- (2) The withholding certificate must be completed with respect to any item on the form that is relevant to the claim made by the account holder and must not contain claims that are inconsistent with claims made in any part of the form.
- (3) If the withholding certificate provides an address that is subject to a hold mail instruction as the account holder's permanent residence address, certain documentary evidence must be provided to support the account holder's claim of foreign status or entitlement to treaty benefits (as applicable).

4.10.21.9.5
(09-20-2018)

Account Review

- (1) The following should generally be requested for each account reviewed:
 - a. Withholding certificates, or documentary evidence (for offshore obligations)
 - b. Mailing and residence addresses from master files
 - c. Information supporting the account holder's status as an individual, corporation, or other entity, and Chapter 4 status for an entity (e.g., as an FFI or NFFE)
 - d. Authorization for certain transactions (i.e., buy or sell stock)
 - e. Other account instructions and correspondence (such as hold mail or, for an offshore obligation, standing instructions)
 - f. Account application forms and updates
 - g. Any other account file information or information needed to administer or open the account

4.10.21.9.6
(09-20-2018)

Validation Process

- (1) It is recommended that the validation of Form W-8 be performed in three steps:
 - a. Line-by-line review to ensure that the form is complete and consistent on its face. Note that a failure on any one line item does not necessarily invalidate the certificate and all claims made therein. However, the examiner should consider such failures carefully and shall take special caution in the case of systemic failures. The examiner should exercise sound judgment in applying these guidelines. Avoid focusing on insignificant failures. The absence of a foreign or U.S. TIN when either is required is not an insignificant failure.
 - b. Comparison of information on the Form W-8 with the information in the account file and/or account application form. A material contradiction may invalidate the Form W-8, based on the reason to know and actual

knowledge standards. In this connection, the examiner should review account file information and new account application forms and updates for indication of U.S. status (e.g., a U.S. mailing address, a copy of a U.S. driver's license used as identification to open the account, or a U.S. birthplace indicated on a passport), a hold mail instruction, or information that would indicate residence in country other than that claimed on the Form W-8 for an account holder making a treaty based claim. See Treas. Regs. 1.1441-7(b)(5) & (6).

Note: There are items that are indicative of U.S. status that may not be on Forms W-8 being reviewed but are in taxpayer's records (e.g., U.S. place of birth, classification as a U.S. person on records, U.S. telephone number, etc.)

- c. Check of expiration of Form W-8 to ensure it is valid with respect to the applicable payment. See Exhibit 4.10.21-6.
- (2) Other validation points to consider when reviewing Forms W-8 include the following:
 - a. Information on the form against records or file reviewed (if available) – for example, check name on records matches name on form and that a Chapter 3 status is reasonable.
 - b. Check that there is a U.S. TIN when one is required.
 - c. Check treaty claim to see if there is a treaty with the country listed in that section.
 - d. Check treaty claim to see that all required information for treaty claim is provided (e.g., TIN (when required), treaty claim section, specific LOB provision if entity, etc.).
 - e. Check that there is a Chapter 3 status (and Chapter 4 status and GIIN if a withholdable payment is made to an entity).
 - f. Check that the form is signed and dated (if not dated there is a date stamp).
 - g. Check that the correct version of the form was used (revision date) (see Treas. Reg. 1.1441-1(e)(4)(viii)(C)).
 - h. Check the foreign TIN (or reasonable explanation for absence) and date of birth for direct accounts (i.e., not held by intermediaries or flow through entities) held at U.S. offices.

4.10.21.9.7
(07-29-2008)
**Permanent and Mailing
Address Considerations**

- (1) The examiner should pay special attention to the address lines on the withholding certificates and the addresses otherwise reported by the account holder or shown in the account files and customer master files. See Treas. Reg. 1.1441-7(b)(5).

4.10.21.9.7.1
(09-20-2018)
**Permanent Address
Form W-8**

- (1) A person's permanent residence address is an address in the country where the person claims to be a resident for purposes of that country's income tax. In the case of a certificate furnished to claim a reduced rate of withholding under an income tax treaty, the residence must be determined in the manner prescribed under the applicable treaty. See Treas. Reg. 1.1441-6(b) and 1.1441-7(b)(6)(i).
- (2) The examiner should check addresses indicated on records such as the customer master files, which may include changes in circumstance (i.e., new U.S. addresses or addresses outside treaty country) that have not been considered by the withholding agent for updating its certification forms.

4.10.21.9.7.2
(09-20-2018)

**Permanent Residence
and Mailing Address
Cures Using Additional
Documentation**

- (1) The U.S. withholding agent can rely on a Form W-8 with a defective address (i.e., one that renders the Form W-8 unreliable) to establish foreign status if it has obtained certain information or documentation as prescribed in Treas. Reg. 1.1441-7(b)(5)(i). Examples of such additional documentation for different types of taxpayers are in the following paragraphs. See the Instructions for the Requester of Forms W-8BEN, W-8BEN-E, W-8ECI, W-8EXP, and W-8IMY for further information on curing W-8 series forms.
- (2) For individuals:
 - a. A valid identification issued by an authorized government body that is typically used for identification purposes that does not contain a U.S. address (e.g. passport, driver license), and
 - b. A reasonable written explanation from the account holder supporting foreign status.
- (3) For entities:
 - a. Documentation establishing foreign status that substantiates that the entity is organized or created under the laws of a foreign country. For a payment made with respect to an offshore obligation, see Treas. Reg. 1.1441-7(b)(5)(i)(B)(2).
 - b. The figure below shows examples of documentation which can be accepted for an entity:

Entity Documentation
Corporation: Articles of Incorporation
Partnership: Partnership Agreement
Trust: Trust Agreement

Figure 4.10.21-1

Note: More specific rules apply with respect to a treaty claim as the withholding agent must have documentation supporting residency in the treaty country. See Treas. Reg. 1.1441-7(b)(6).

4.10.21.9.7.3
(03-23-2023)

**Forms W-8 Provided
After Date of Payment**

- (1) An examiner should pay special attention to a withholding certificate that was provided after the date of payment. Such a withholding certificate is acceptable if it contains an affidavit that states that the information on the withholding certificate was accurate at the time of payment, and, if the certificate is a Form W-8ECI, the information described in (2) below. The affidavit should be signed by the payee under penalties of perjury and dated. It can be added to the bottom of the form or on a separate page attached to the form.

Note: If the withholding certificate is obtained within 30 days from the date payment was made, the affidavit is not required (including for Forms W-8ECI). See Treas. Reg. 1.1441-1(b)(7)(ii).

- (2) If the withholding certificate is received more than a year after the date of payment, the withholding certificate is acceptable if, in addition to the affidavit, the withholding agent obtains documentary evidence that supports claim of foreign status and or treaty claim. Examples of acceptable documentary

evidence supporting a claim of foreign status includes: an individual's government identification which does not contain a U.S. address or a certificate of incorporation from a foreign country. See Treas. Reg. 1.1471-3(c)(5)(i). Documentary evidence supporting an individual's treaty claim includes any government issued identification that includes the individual's name, address, and photograph that has been issued no more than three years prior to presentation to the withholding agent. If older than three years, additional evidence of the person's residence in the treaty country is needed (i.e., a bank statement, utility bills, or medical bills). See Treas. Reg. 1.1441-6(c)(4)(i). For entities, the documentary evidence needed includes any official government document that includes the name of the entity and the address of its principal office in the treaty country. See Treas. Reg. 1.1441-6(c)(4)(ii).

- (3) If the withholding certificate that is provided after the date of payment is a Form W-8ECI, Certificate of Foreign Person's Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States, the affidavit must include certain information regarding the inclusion of that income in the recipient's U.S. income tax return. Specifically, in addition to indicating that the information and representations contained on the certificate were accurate at the time of the payment, it must indicate that either (i) the beneficial owner has included the income on its U.S. income tax return for the taxable year in which the income must be reported, or (ii) the beneficial owner will include the income on its U.S. income tax return for the taxable year in which the income must be reported and the due date for filing the return (including any applicable extensions) is after the date on which the affidavit is signed. See Treas. Reg. 1.1441-1(b)(7)(ii)(B).
- (4) The examiner may consider, among other factors, the following factors in determining whether a withholding certificate received after the date of payment (or other documentation or documentary evidence if the payment is made with respect to an offshore obligation) should be accepted for purposes of allowing a reduced withholding rate with respect to payments to foreign persons:
 - a. Whether information and representations on a later secured withholding certificate (or on other documentation if it is an offshore obligation) provided are consistent with information in the account file or in other records maintained by the withholding agent. The examiner should request and review all account files as a result.
 - b. Whether the withholding certificate (or other documentation if it is an offshore obligation) establishes facts in existence at the time the relevant payments were made.

4.10.21.9.7.4
(03-23-2023)

When a Withholding Agent Receives an Unreliable Form W-8ECI

- (1) Under ordinary circumstances, absent actual knowledge or reason to know otherwise, a withholding agent may rely on a claim of exemption (for effectively connected income) if, prior to the payment to a foreign person, the withholding agent can reliably associate the payment with a Form W-8ECI, Treas. Reg. 1.1441-4(a)(2)(i).
- (2) If an examiner determines that Form W-8ECI is unreliable because the person has not reported the income identified on the form, the examiner should contact the Foreign Payments Practice (FPP) Program Office, Team 1190 manager regarding unreliable Form W-8ECIs.
- (3) Notification to Withholding Agent - The examiner may be able to determine and then notify the withholding agent that the Form W-8ECI being used is unreli-

able and can no longer be honored and therefore they should begin withholding at 30%. If appropriate, Counsel will draft a letter to the withholding agent which will serve as the notification of the unreliable Form W- 8ECI. The letter will inform the withholding agent that it can no longer accept Form W- 8ECI from this particular recipient. Due to IRC 6103, the reason why the Form W-8ECI is unreliable may not be disclosed to the withholding agent.

- a. If the foreign person submitted Forms W-8ECI to other withholding agents, the examiner cannot disclose the foreign person's filing status to these other agents.
 - b. The examiner should consult with Counsel if they are contemplating providing any other information about the payee in question to the withholding agent.
- (4) At the time that the notification letters are issued, the examiner will complete a Form 3870, Request for Adjustment, and submit the form to the manager who will forward it to the proper individual for processing. This will enable the issuance of the notification letter to appear on the withholding agent's transcript. A separate Form 3870 must be prepared for each unreliable Form W-8ECI. The information needed in the Form 3870 request includes:
- a. Withholding Agent 1042 module (EIN, TY, and MFT 12)
 - b. Transaction Code - 971, Action Code - 710
 - c. Recipient's TIN, RECIP Name Control (4 characters), and 20 characters to note date letter was received.
- (5) For future cycles, examiners should confirm that withholding agents who have been issued letters are now withholding tax with respect to payments to the particular recipient. If the withholding agent has ceased making payments to that particular recipient, no withholding tax is due.

4.10.21.9.8
(09-20-2018)
**Use of Statistical
Sampling**

- (1) An audit of a U.S. Withholding Agent usually involves a review of Withholding Certificates, account holder Information, and other associated documentation. This review will often require statistical sampling due to the volume of potential sampling units such as number of accounts, payments, Forms 1042-S issued. Additionally, reviews of potentially complicated financial transactions could also necessitate the use of statistical sampling. CAS should be involved in decisions concerning statistical sampling, and therefore a referral for CAS assistance should be made very early in the process. CAS involvement is necessary for both designing and projecting a statistical sample, however, the Auditor's Workbench – IRMF (AW-I) software package can be used by a non-CAS field agent without assistance, to create a population of Forms 1042-S filed with the IRS, based on a risk calculation of maximum potential under-withholding $[(\text{Gross Income Amount} * 30\%) - \text{Amount Withheld}]$. For the details on the statistical sampling process please refer to the future IPS unit "FDAP Payments – Statistical Sampling and Projection Procedures". For a more thorough treatment of statistical sampling audit techniques not specifically targeted at audits of U.S. withholding agents, please refer to IRM 4.47.3, Statistical Sampling Auditing Techniques.
- (2) The starting point for sampling the foreign payments of a U.S. withholding agent should be an analysis of the withholding agent's business and associated systems, intended to ensure that all applicable payments and payees are

processed through their withholding and reporting systems. This is particularly important when the sampling unit is a Form 1042-S, or a sampling unit derived from such forms.

(3) Potential sampling units to consider in developing a sampling plan include:

- a. Form 1042-S
- b. Account holders
- c. Accounts
- d. Payments

Regardless of the sampling unit chosen, withholding certificates, account file information and any other relevant information potentially affecting the determination of the rate of withholding should generally be evaluated for every sample unit selected for review.

(4) While the use of statistical sampling as an audit tool by the IRS does not require the approval of the taxpayer (withholding agent), the FPP agent and CAS should request the withholding agent review the sampling plan to provide input to improve its efficiency or raise other issues. Input may include, but is not limited to, determining the population, the sampling unit, sample size and stratum criteria.

(5) In almost all sampling situations a stratified sample will be used. Stratification usually results in a more efficient sample than a simple random sample. It also allows concentration on specific sample units that the auditor feels have a higher risk than other sample units. The most common, and generally recommended factor used in determining stratum boundaries is the previously mentioned risk calculation. Additional factors to consider when determining strata boundaries include:

- a. Lines of business
- b. Type of income (as defined per Form 1042-S income codes)
- c. Type of exemption (as defined per Form 1042-S exemption codes)
- d. Status codes per Form 1042-S
- e. Beneficial owner vs. intermediary or flow-through accounts/recipients
- f. Direct vs. indirect accounts
- g. Type of withholding certificate W-8 (BEN, BEN-E, EXP, ECI or IMY) Form 8233, or Form W-9
- h. Withholding tax rates
- i. Type of transaction (IRM 4.10.21.9.10)
- j. Recipient's country of residence for tax purposes per Form 1042-S

(6) Examiners are encouraged to use Auditor's Workbench IRMF (AW-I) as a tool for determining the sample population. The sample unit used by AW-I is Form(s) 1042-S filed with the IRS, obtained through the Information Returns Master File. The examiner can filter the population and eliminate no risk or low risk pools, where risk is defined as $[(\text{Gross Income Amount} * 30\%) - \text{Amount withheld}]$. A population file is created and sent to a CAS, who imports the population into a statistical sampling program to create a stratified sample. The CAS will send the sample file back to the examiner, which is imported back to AW-I. Audit results can then be recorded in AW-I and sent to the CAS to calculate the resulting adjustment/projection. AW-I is not applicable to populations not based on Forms 1042-S, such as audits of payments to foreign vendors. See IRM 4.10.21.10.3, Payment to Foreign Persons (Payees) - Three-Step Audit Procedure.

4.10.21.9.9
(09-20-2018)
**Withholding and
Reporting Verification**

- (1) In determining the correct rate of withholding and backup withholding for a single payment or group of similar payments, account documentation, applicable presumption rules, type of payment being made, and any applicable tax treaties or Code exemptions should first be taken into account. Once the correct rate of tax is determined based on these factors, steps should be taken to ensure the correct rate was applied for withholding purposes, and that amounts withheld were accurately reported on Forms 1042-S or Forms 1099, as applicable. In instances where additional NRA withholding, additional backup withholding, or assessment of penalties results from the use of a statistical sample, the results should be extrapolated to the sample population where appropriate. These will be discussed in future IPS unit "FDAP Payments – Statistical Sampling and Projection Procedures".
- (2) To this end, account statements and similar records that show the type of income earned and tax withholding should be obtained for each applicable payment and the associated payees. Account records that show how the withholding agent has classified payments along with records that show how those same payments were classified by the payee of the income to the withholding agent may also be requested.
- (3) Copies of all Forms 1042-S and Forms 1099 filed by the withholding agent to report all payments under review should be obtained, preferably from IRS systems, to ensure proper reporting, including cases in which the examiner is not proposing any change to the withholding rate. If examiners are unable to reconcile information reported by a taxpayer, such as what is reported on F1042 and F1042-S, then they may request that taxpayer provide the information regarding Forms 1042, 1042-T and 1042-S from taxpayers in FIRE ready ASCII format, or in an Excel spreadsheet. All information appearing on Forms 1042-S that might affect withholding tax (e.g., income codes and amounts, exemption codes, recipient code, recipient country for tax purposes, amounts repaid to account holders, etc.) should also be reviewed for accuracy and completeness, and should be compared to the documentation reviewed by the examiner. Payment transcripts should tie to withholding agent deposit workpapers. Liability dates reported on Form 1042 should tie to dates that the withholding agent made deposits into account holders' accounts. In cases where the withholding agent is a large entity, statistical sampling should be considered.

4.10.21.9.10
(07-29-2008)
**Transactions and Other
Items Requiring Special
Treatment by
Withholding Agents**

- (1) NRA withholding and reporting for the transactions listed below require application of special rules. For the withholding agent to comply with these requirements, the withholding agent should establish procedures to identify and to ensure the correct withholding and reporting for each type of transaction. After identifying their existence, the examiner should ask the taxpayer for a detailed explanation of the withholding and reporting procedures for each of these types of transactions. If the procedures are deficient or incomplete, the examiner should expand the examination to ensure that the transactions were properly reported and that taxes were properly withheld.

4.10.21.9.10.1
(09-20-2018)
**Qualified Investment
Entity (including Real
Estate Investment Trust
(REIT) Distributions**

- (1) REIT distributions to foreign shareholders are subject to NRA withholding, except when the distribution is designated as a capital gain dividend, a return of basis, or a distribution of more than the shareholder's basis in the REIT stock. Treas. Reg. 1.1441-3(c)(4)(i)(C). For capital gain dividends, a 21% withholding tax applies under IRC 1445 (35% for 2017 and prior years). See IRC 1445(e)(6) and Treas. Reg. 1.1445-8. As enacted under the American Jobs

Creation Act of 2004, however, capital gain distributions are not taxed under IRC 1445 for foreign shareholders owning REIT stock regularly traded on a U. S. exchange that have not held more than 10% of such class of REIT's stock (5% for dispositions before December 18, 2015). Such distributions are instead subject to NRA withholding. Also, a "qualified foreign pension fund" is not subject to withholding under IRC 1445 on the capital gain dividend portion of a distribution by a REIT. The examiner should question how the withholding agent determines the correct withholding rate and should spot check several REIT (or RIC) distributions.

- (2) Generally, similar rules apply to a Regulated Investment Company (RIC) that is a "Qualified Investment Entity" (see IRC 1445(e)(6)).

4.10.21.9.10.2
(09-20-2018)

**Original Issue Discount
(OID)**

- (1) Generally, NRA withholding applies to the redemption of OID debt obligations whenever a calculation of OID is included in the amount of the redemption. The portfolio interest exemption or treaty reductions may reduce or eliminate the NRA withholding tax. Redemptions of obligations that carry OID are subject to withholding tax whether the redemptions are early or as originally scheduled. The amount subject to withholding tax is the amount accrued to the holder from the date of purchase, as determined by the withholding agent, reduced by any amount of OID that was considered prior to that time (due to a payment made on the obligation).
- (2) If the withholding agent has not been provided with reliable date of purchase information or cannot otherwise calculate the amount of OID that accrued to the holder, then the withholding agent must withhold on the entire amount of OID accrued since the obligation's issuance until the date of redemption. In determining the taxable amount of OID, a withholding agent may rely on information provided in Pub 1212, List of Original Issue Discount Instruments. The amount of taxable OID (including OID that is portfolio interest) is reportable on Form 1042-S. Short-term OID (i.e., on an obligation with a maturity of 183 days or less from the date of original issue) is not subject to NRA withholding tax or reporting on Form 1042-S. Banks and brokerages often use an outside service to compute the annual OID on marketable securities as the information is required for 1099 reporting to U.S. residents.

4.10.21.9.10.3
(09-20-2018)

Securities Lending

- (1) When a loan of securities is outstanding during the record date for a dividend or interest payment, the lender of the securities is, among other things, typically entitled to a payment from the borrower to account for the foregone dividend or interest (i.e., since the lender is not the holder of record on the record date). The payment made by the borrower of securities is called a "substitute dividend" or "substitute interest", which may be subject to NRA withholding tax if paid to foreign persons.
- (2) A "look-through" rule applies to define the character and source of the substitute amount paid relating to the loan of any securities. Based on the "look-through" rule, a substitute interest amount is treated as portfolio interest for NRA withholding purposes if the underlying security generates portfolio interest regarding the payment. These rules further apply to security lending transactions between foreign counterparties, subject to provisions to mitigate over-withholding that could result from repeated lending of the same underlying security. See Notice 2018-5, 2018-6 I.R.B. 341.

- (3) Any substitute dividend payments made pursuant to a securities lending transaction, sale-repurchase, or a substantially similar transaction that references an underlying security is a dividend equivalent. An underlying security is any interest in an entity that could give rise to a U.S. source dividend, considering rules for derivatives that reference partnership interests. As a dividend equivalent, the substitute dividend payment is treated as U.S. source dividend that is subject to withholding.
- (4) A financial institution may borrow securities for short sales or when sellers fail to deliver securities in sales transactions. As a borrower, the financial institution is responsible for any withholding required on payments to the lender. A financial institution may also act as an intermediary or counterparty in securities lending transactions between unrelated counterparties. If a financial institution that is a custodian loans a security of its customer that is a foreign person, it is responsible for any withholding on subsequent payments made to the customer.

4.10.21.9.10.4
(09-20-2018)
**Overnight Deposits
(Sweep Accounts)**

- (1) Commercial banks sometimes offer their larger accounts preferred treatment. One of these benefits is earning interest on the balance at the close of the business day. Typically, the balances are combined and used to purchase interest bearing securities. The next business day the interest earned is credited to the customer's account.

4.10.21.9.10.5
(09-20-2018)
**Repurchase Agreements
(REPOs)**

- (1) Under U.S. tax principles, a REPO is typically characterized as a collateralized loan where the purchaser of the underlying security is deemed to be a lender of funds to the seller in the amount of the purchase price. The seller of the security is treated as the borrower. The loan is for the period until the REPO matures, when the securities are sold back to the original seller (i.e., the cash borrower). Typically, the repurchase price exceeds the original sales price, giving rise to a charge treated as financing interest.
- (2) If the financing interest is U.S. sourced and paid to a foreign person, it may be subject to NRA withholding. See Treas. Reg. 1.1441-2(a)(3), (5) and (6) for exceptions from withholding that may apply. In addition, an examiner may find substitute payments (dividend or interest) made by the cash lender to the borrower as part of the REPO. These substitute payments are like those typically seen in securities lending transactions, whose sourcing is determined with respect to the underlying security for withholding and reporting purposes. See the Securities Lending section and IRC 1058 for more information.
- (3) Financial institutions engage in REPOs for obtaining or making short-term financing or for acting as dealers in transactions between unrelated counterparties (including so-called "tri-party" REPO transactions made to support the obligations of the counterparties).

4.10.21.9.10.6
(09-20-2018)
**Notional Principal
Contracts (NPC)**

- (1) Except as provided in (2) below, there is no NRA withholding obligation on payments made under NPCs described in Treas. Reg. 1.863-7(a) or 1.988-2(e) to foreign persons because the income is foreign source income. See Treas. Reg. 1.1441-4(a)(3). However, if these payments are ECI or presumed to be ECI as to the foreign person, the withholding agent is required to report such payment on Form 1042-S indicating the exemption from withholding because it is ECI. See Treas. Reg. 1.1441-4(a)(3). A withholding agent must presume the payments as ECI if the income is paid to, or to the account of, a qualified business unit of a foreign person located in the U.S. If the payment is paid to,

or to the account of, a qualified business unit of a foreign person located outside the U.S., the income must be treated as ECI if the withholding agent knows or has reason to know that the income relates to the conduct of a trade or business within the U.S. The ECI presumption may be rebutted by a withholding certificate representing that the payments are not effectively connected with the conduct of a U.S. trade or business. Instead of a withholding tax certificate, a payee may represent in a master agreement governing the transactions in NPCs between the parties that the counterparty is a U.S. person or a non-U.S. branch of a foreign person. Income on NPCs that is regarded as embedded interest or recharacterized as certain other payments under U.S. tax principles might be subject to NRA withholding and reporting.

- (2) There is NRA withholding obligation on payments under an NPC when the payment references a dividend from an underlying security and the NPC is a specified notional principal contract (SNPC). Those payments are dividend equivalents under IRC 871(m). Treas. Reg. 1.871-15(c)(ii). An underlying security is any interest in an entity that could give rise to a U.S. source dividend, considering rules for derivatives that reference partnership interests. See Treas. Reg. 1.871-15(a)(15) and (m). As a dividend equivalent, the payment pursuant to the SNPC that references the payment of a dividend is treated as a U.S. source dividend that is subject to withholding. A withholding agent is required to withhold on the amount of the payment that is a dividend equivalent. Treas. Reg. 1.1441-7(a)(2). A specified NPC may include other payments that are not dividend equivalents. For those payments, there is no NRA withholding obligation on payments made under NPCs described in Treas. Reg. 1.863-7(a) or 1.988-2(e) to foreign persons. See Treas. Reg. 1.1441-4(a)(3).
- (3) A financial institution engages in SNPC transactions when acting in a dealer capacity or for taking proprietary long and short positions in underlying securities (or as hedges of other transactions).

4.10.21.9.10.7
(09-20-2018)
**Equity-Linked
Instruments (ELI)**

- (1) There is NRA withholding obligation on payments under an ELI when the payment references a dividend from an underlying security and the ELI is a specified ELI. See Treas. Reg. 1.871-15(c) and (e). An ELI is a financial transaction, other than a securities lending transaction, sale-repurchase transaction, or an NPC, that references the value of one or more underlying securities. Treas. Reg. 1.871-15(a)(4). Examples of an ELI include, but are not limited to, a forward contract, a futures contract, an option, or a structured note. The payments made by that reference to a dividend from an underlying security are treated as dividend equivalents. A dividend equivalent is a U.S. source payment that is subject to withholding. Treas. Reg. 1.871-15(b). A withholding agent is required to withhold on the amount of the payment that is a dividend equivalent. Treas. Reg. 1.1441-7(a)(2). A specified ELI may include other payments that are not dividend equivalents. The withholding obligations for those other payments will depend on the type of instrument and the characterization of those other payments.

4.10.21.9.10.8
(09-20-2018)
Syndicated Loans

- (1) A syndicated loan or loan participation results when financial institutions collectively participate in funding a single loan with a lead bank. In some cases, each participating bank will be considered a direct lender, where in other cases the arrangement may be considered a separate loan between the lead bank and the participating banks (though the separate loan does serve to fund the original loan). Generally, the lead bank will act as an administrator, which will

be the withholding agent. Generally, the Agent Bank maintains records of loan ownership. It processes loan assignments and corporate actions. It collects and pays principal and interest payments and applicable shares of loan fees to lenders that participate in the loan. Thus, the Agent Bank must determine the source and character of the income, collect valid U.S. tax forms from the lenders and apply the correct rate of U.S. withholding tax and/or exemption where applicable. The following issues should be considered related to syndicated loans/loan participations:

- a. **Bank loan exception:** IRC 871(h) and IRC 881(c) generally provide that a non-U.S. person is exempt from the 30 percent NRA withholding tax on portfolio interest. There are several limitations on this exemption. One is the “bank loan exception”. The portfolio interest exemption does not apply to any U.S. source interest received by a bank on the extension of credit made pursuant to a loan agreement entered in the ordinary course of its trade or business. See IRC 881(c)(3)(A). Accordingly, foreign banks, who are participants in a syndicated loan, should not generally benefit from the portfolio interest exemption. As a result, the examiner should consider whether the arrangement should be properly treated as a direct loan made by each participating foreign bank in cases in which the lead bank is a foreign bank.
- b. **Change in participants to the loan:** Often the participants will change. For example, when the original participants sell all or a portion of their interests in the loan to another bank, withholding related documentation is required from the new participants.
- c. **Required NRA withholding agent’s responsibilities:** An audit concern is to determine if required Forms 1042 and 1042-S were not filed and/or Forms W-8 were not secured from the participating banks.

4.10.21.9.10.9
(03-23-2023)

Payments to Foreign Intermediaries and Foreign Flow-Through Entities

- (1) Reportable amounts that withholding agents pay to foreign intermediaries or foreign flow-through entities require specific treatment because intermediaries and flow-through entities are not beneficial owners of income. Examples of flow-through entities are foreign partnerships, foreign simple and foreign grantor trusts, and, for payments for which a reduced rate of withholding is claimed under an income tax treaty, any entity to the extent it is considered to be fiscally transparent with respect to the payment by an interest holder’s jurisdiction.
- (2) Foreign intermediaries and flow-through entities must provide the financial institution withholding agent a Form W-8IMY. This form indicates that the entity is not the beneficial owner of the reportable amount. The form also indicates if they have entered into an agreement with the IRS to act as a withholding agent (i.e., qualified intermediary, withholding foreign partnership or withholding foreign trust) for certain payments.
- (3) Foreign financial institutions and certain intermediaries that are non-financial entities can enter into an agreement with the IRS to act as a qualified intermediary (QI). All foreign intermediaries, who do not have an agreement with the IRS to act as QIs are, by default, non-qualified intermediaries (NQIs). See Rev. Proc. 2017-15.
- (4) Foreign partnerships, foreign simple or foreign grantor trusts, can elect to enter into an agreement with the IRS to become a withholding foreign partnership (WP) or a withholding foreign trust (WT). A foreign flow-through entity that has

not become a WP or a WT is, by default, a nonwithholding foreign partnership (NWP) or a nonwithholding foreign trust (NWT). See Rev. Proc. 2017- 21.

4.10.21.9.10.9.1
(09-20-2018)

**Withholding and
Reporting on Payments
to Qualified Intermediary
(QI)**

- (1) The QI can elect whether or not to assume primary withholding responsibilities. The U.S. withholding agent will be notified about this decision with a valid Form W-8IMY (and, if needed, a withholding statement that includes the QI's Chapter 4 status) that the QI furnishes to the withholding agent for purposes of Chapters 3 and 4 and IRC 3406.
- (2) Under the QI agreement with the IRS, the QI is required to designate the accounts that are covered under the QI agreement on Form W-8IMY or a withholding statement. For accounts that the QI did not designate as covered by the QI agreement, the below described NQI procedures shall be followed. A QI must generally provide a withholding statement to identify the payments for which it acts as a QDD. To the extent that a QI acts as Qualified Derivatives Dealer for payments associated with a valid Form W-8IMY, the QI assumes primary withholding responsibility for payments with respect to potential section 871(m) transactions.
- (3) To the extent the QI has assumed primary withholding responsibilities, the U.S. withholding agent is not required to withhold taxes with respect to those payments associated with QI-designated accounts. However, it is still subject to reporting on these. The U.S. withholding agent will report payment amounts paid to the QI with respect to such accounts on Form 1042-S with 0% taxes withheld. These Form(s) 1042-S will be issued to the QI by the U.S. withholding agent. The QI will be responsible for the withholding and reporting on Form 1042-S with respect to its account holders. The QI can generally file Forms 1042-S on a pooled reporting basis (instead of issuing separate Forms 1042-S to each account holder), subject to the exceptions provided in the QI agreement.
- (4) To the extent the QI has not assumed primary withholding responsibilities, the U.S. withholding agent will withhold and report on Forms 1042-S based on withholding statements provided by the QI with respect to QI-designated accounts. The QI is not generally required to provide specific client names and client details to the withholding agent. Instead, the QI will provide the U.S. withholding agent a withholding statement that indicates the income amount and amounts to be withheld by the USWA on a pooled basis (grouping foreign and U.S. exempt account holders by income type, withholding tax rates, such that, for example, dividends subject to withholding at the 15% withholding rate would be one pool and dividends subject to withholding at the 30% withholding rate would be another pool). A reporting pool for Chapter 4 purposes (Chapter 4 withholding rate pool) might instead be provided. See Treas. Reg. 1.1471-1(b)(20).

4.10.21.9.10.9.2
(09-20-2018)

**Withholding and
Reporting for Payments
to Non-Qualified
Intermediary (NQI)**

- (1) An NQI should provide to the withholding agent a Form W-8IMY and the appropriate documentation (i.e., Form W-8BEN/BEN-E/etc. or Form W-9 or documentary evidence) for each of the beneficial owners that are to receive the income paid by the withholding agent to the NQI, except for payments allocable to a Chapter 4 withholding rate pool. The NQI must also provide a withholding statement to the withholding agent for allocating payments of income to the beneficial owners (or applicable Chapter 4 withholding rate pools) and for determining the applicable withholding tax rates. If the NQI has provided all the above information, the U.S. withholding agent should withhold

and report based on the information provided by the NQI. Information reporting is made by the withholding agent to each beneficial owner or Chapter 4 withholding rate pool on a separate Form 1042-S.

- (2) If the NQI does not provide the above information to the U.S. withholding agent, the U.S. withholding agent must apply the appropriate presumption rule to determine the required withholding. The portion of the payment for which no documentation or allocation information was provided, will be treated as allocated to unknown recipient and subject to 30% withholding tax. There may be partially documented beneficial owners for which the withholding agent will withhold based on the allocation information and documentation provided and report on Form 1042-S accordingly. For the portion of the payment that is treated as made to unknown recipient and subject to 30% withholding, the withholding agent will issue a Form 1042-S to an unknown recipient listing the intermediary in the intermediary/flow-through entity box.
- (3) An NQI is generally not required to withhold and report if it has provided all the required documentation (Form W-8IMY including withholding statement and documentation for each underlying investor) to the withholding agent. However, the NQI will be required to withhold and report under Chapter 3 if it knows or has reason to know that another withholding agent failed to withhold the correct amount or failed to report the payment correctly.
- (4) An NQI that is a NPFFI is itself subject to FATCA withholding. For this reason, an NQI must identify its Chapter 4 status on Form W-8IMY. The U.S. withholding agent would report the withholding as under Chapter 4 on Form 1042-S, with the payment treated as made to an unknown recipient, listing the intermediary in the intermediary/flow-through entity box.

4.10.21.9.10.9.3
(09-20-2018)

Withholding and Reporting for Payments to Withholding Foreign Partnership/Withholding Trust (WP/WT)

- (1) U.S. withholding agents generally do not withhold taxes on a foreign partnership or trust that has provided a valid Form W-8IMY indicating their status as a withholding foreign partnership (WP) or a withholding foreign trust (WT) and provides a valid Chapter 4 status. WPs and WTs must assume primary withholding responsibilities for payments to partners, beneficiaries or owners when receiving payments in their capacity as WPs or WTs. The income paid to the WP or the WT will be reported on Form 1042-S to the WP or WT as the recipient with 0% taxes withheld. The WP/WT will be responsible for the withholding and reporting on Form 1042-S with respect to its partners, beneficiaries or owners. WP/WT can file Form 1042-S on a pooled reporting basis (instead of issuing separate Forms 1042-S to each partner, beneficiary, or owner) for its partners, beneficiaries, or owners, subject to the exceptions provided in the WP or WT agreement.

4.10.21.9.10.9.4
(09-20-2018)

Withholding and Reporting for Payments to Non-Withholding Foreign Partnership/Non-Withholding Foreign Trust (NWP/NWT)

- (1) The treatment of a non-withholding foreign partnership (NWP) or a non-withholding foreign trust (NWT) is generally like the treatment of a NQI. The NWP or NWT should provide the withholding agent with Form W-8IMY (including the NWP's or NWT's Chapter 4 status), documentation for each partner, beneficiary, or owner, and a withholding statement containing certain information on each partner, beneficiary, or owner and an allocation of each payment to each such payee to the extent required under the Chapter 3 regulations (in lieu of an allocation to a pool of payees, except for a Chapter 4 withholding rate pool). If the NWP or the NWT does not provide the above information to the U.S. withholding agent, the withholding agent must generally withhold in accordance with the applicable presumption rule.

4.10.21.9.10.9.5
(09-20-2018)

**Withholding and
Reporting on Payments
to a Disregarded Entity
(DE)**

- (1) In general, a foreign business entity (other than a “per se” corporation) that has a single owner may be disregarded as an entity separate from its owner (a disregarded entity) for federal income tax purposes. The payee of a payment made to a disregarded entity is the owner of the entity.
- (2) **U.S. Source Payment to DE with Foreign Owner** – If the owner of the entity is a foreign person, the withholding agent must apply withholding, generally at a 30% tax rate, unless the foreign owner can be treated as a beneficial owner entitled to a reduced rate of withholding.
- (3) **U.S. Source Payment to DE with U.S. Owner:**
 - a. If the owner of a DE is a U.S. person, the withholding agent does not apply Chapter 3 or 4 withholding. However, the withholding agent may be required to report the payment on Form 1099 and, if applicable, backup withhold. A withholding agent must assume that a foreign entity is not a disregarded entity unless it can reliably associate the payment with documentation provided by the owner or has actual knowledge or reason to know that the foreign entity is a disregarded entity.
 - b. A payment from the U.S. owner to a DE that is a foreign entity is not subject to NRA withholding because the DE’s income is included in the U.S. owner’s tax return. The DE’s activities are treated as a sole proprietorship (if the owner is an individual), or as a branch or division of the owning entity.

4.10.21.9.11
(09-20-2018)

**Portfolio Interest for
Registered Obligations**

- (1) IRC 871(h)(1) and 881(c)(3) generally exempt from NRA withholding interest payments (including OID) on registered obligations that qualify as portfolio interest.
- (2) An obligation is registered when it meets the requirements specified in Treas. Reg. 1.871-14(c). The withholding agent must also obtain a withholding certificate or documentary evidence that the beneficial owner of the interest payment is not a U.S. person to treat the interest as portfolio interest. This documentation requirement does not apply in cases of foreign targeted registered obligations, which have separate requirements and which only apply to registered obligations issued before January 1, 2016. See Treas. Reg. 1.871-14(e).

4.10.21.9.11.1
(09-20-2018)

**Foreign Targeted Bearer
Obligations**

- (1) Foreign targeted debt in bearer form issued before March 19, 2012 may also qualify for the portfolio interest exemption if it meets certain requirements. See IRC 871(h)(2) and IRC 881(c)(2).
- (2) A bearer obligation is one that is not in registered form. The bearer obligation is foreign targeted when it meets the following three requirements:
 - a. There are arrangements to ensure that the obligations are not sold to U.S. persons.
 - b. Payment of interest is made outside the U.S. and its possessions.
 - c. The face of the obligation states that any U.S. person who owns the obligation will be subject to U.S. taxation. See IRC 163(f)(2).
- (3) None can be issued after March 18, 2012 per the HIRE Act.

4.10.21.9.11.2
(09-20-2018)

Exceptions

- (1) The following are interest income payments that do not qualify for the portfolio interest exemption even when the interest is paid with respect to a registered or foreign targeted bearer obligation:

- a. Interest which is paid to a foreign person who owns directly or indirectly 10 percent or more of the entity paying the interest
- b. Interest which is paid to a foreign bank on the extension of credit made pursuant to a loan agreement entered in the ordinary course of the bank's trade or business
- c. Interest which is paid to a foreign controlled corporation from a person related to that foreign controlled corporation
- d. Contingent interest paid to a foreign person such that payments resemble dividends

4.10.21.9.12
(09-20-2018)

**U.S. Financial Institution
– Consideration of
Payments to Foreign
Persons**

- (1) Many U.S. financial institutions are multinational corporations that make payments to foreign persons in a proprietary capacity that are outside the conduct of a financial services business. Therefore the examiner should review their payments to foreign vendors and other related and unrelated foreign persons for possible withholding tax and reporting requirements. See IRM 4.10.21.10, Nonfinancial Institution Withholding Agent Audit.

4.10.21.9.13
(07-29-2008)

**Suggested Initial
Information Document
Requests (IDR)**

- (1) These information document requests are provided as a general guide to the examiner. It is recommended that they be adapted by the examiner to fit the needs of the audit. An example of how some of these requests may be addressed in an IDR is illustrated in Exhibit 4.10.21-4, Sample IDR for Audits of Financial Services Companies.
 - **Request # 1:** The examiner should request copies of Forms 1042 and Forms 1042- S, along with supporting documentation.
 - **Request # 2:** The examiner should request information relating to policies and procedures of fiduciary (custodial) accounts. Areas covered should include account opening, documentation validation, renewal of Forms W-8, sourcing and characterization of income. The examiner should consider requesting operating manuals, and interviewing relevant personnel.
 - **Request # 3:** The CAS, with the assistance of the examiner, should attempt to identify all systems involved in any aspect of processing and tracking transactions that are potentially subject to NRA or Chapter 4 withholding and reporting. Some withholding agents may use many different systems, so consideration should be given to requesting data flow diagrams at a system's level.
 - **Request # 4:** The CAS, with the assistance of the examiner, should attempt to identify the systems along with the specific files or tables to be used as sources of information needed to identify all payments potentially subject to NRA or Chapter 4 reporting and or withholding. Special consideration should be given to ensuring all payments requiring special treatment by the withholding agent are accounted for through the custodial systems.

4.10.21.10
(09-20-2018)

**Nonfinancial Institution
Withholding Agent Audit
(Payments of FDAP U.S.
Sourced Income to
Foreign Persons)**

- (1) The audit will focus on entities that make payments to foreign persons that are engaged in nonfinancial business activities (e.g., regarding the use of property). While many types of payments to foreign nonfinancial institutions will be effectively connected to a U.S. trade or business, this IRM focuses on payments that are subject to NRA withholding.
- (2) While not covered in detail in this IRM, payments that are not subject to NRA withholding under IRC 1441-1443 may be subject to withholding under other

Code sections (e.g., IRC 1445 for certain dispositions of U.S. real property interests) and reported on Form 1042. In addition, payments that are income effectively connected to the conduct of a trade or business within the U.S. generally are not subject to NRA withholding (e.g., payments for services performed by a foreign corporation engaged in a U.S. trade or business). Non-financial payments do not fall within the definition of a withholdable payment for Chapter 4 purposes, and therefore no Chapter 4 withholding would apply.

- (3) The examiner would follow an audit trail to understand the nature and the character of the transaction. As discussed below, the examiner would follow the trail from the accounts payable or other payment department to the Form 1042-S issued to the foreign person. The audit trail would continue to the withholding certificates if there is reduced withholding. Overall, the examiner is looking to verify:
- The amount paid is consistent with the amount reported on Form 1042-S
 - The income classification of the FDAP income is accurate
 - The address of the beneficial owner is consistent with the treaty exemption claimed
 - Correct income and exemption codes were used on Form 1042-S
 - The correct tax is withheld

4.10.21.10.1
(09-20-2018)
Introduction

- (1) U.S. entities that make FDAP payments to foreign persons generally have NRA withholding and reporting requirements. For example, a large multinational pharmaceutical company pays royalties to a foreign company under a license to sell its drugs within the United States. The royalty payments would typically constitute FDAP income subject to tax under IRC 881(a). The amounts would be withholdable under IRC 1442 as U.S. source FDAP income to a foreign company. Therefore, the income would be subject to reporting (Form 1042 and Form 1042-S) and a NRA withholding tax of 30% absent a valid treaty or ECI claim. The examiner should examine all material payments to foreign persons to determine whether they are U.S. sourced FDAP income payments subject to withholding. The below sections provide a three-step audit procedure to determine payments that may generate NRA withholding and reporting responsibilities.

4.10.21.10.2
(03-23-2023)
**Industries Likely to Have
NRA Withholding and
Reporting**

- (1) The following list is not all-inclusive and is provided so that examiners dealing with one or more of these industries will be aware of the possibility of NRA withholding requirements under IRC 1441 or 1442:
- a. Professional services partnerships: law, accounting, architecture, engineering, etc.
 - b. High tech industries: computer software and hardware providers, medical equipment
 - c. Intellectual products providers: entertainment industry, publishing industry
 - d. Pharmaceutical industry
 - e. Real estate industry
 - f. Daily fantasy sports
 - g. Online advertising

4.10.21.10.3
(09-20-2018)
**Payment to Foreign
Persons (Payees) –
Three-Step Audit
Procedure**

- (1) The examiner can use these procedures to determine if payments made by a U.S. payor to foreign persons require reporting and NRA withholding. Most of these payments will be made to foreign payees by the accounts payable department. Therefore, the examiner should obtain from the taxpayer the following:
 - a. The account payable file and similar files that contains all payments made to foreign payees
 - b. The vendor file (file containing all names and vendor information about the foreign payees)
- (2) In order to determine which payments are subject to reporting and NRA withholding, steps one and two require analysis of the taxpayer's accounts payable file and vendor file. It is recommended that a Computer Audit Specialist (CAS) be requested to assist in each of these three steps:
 - a. Determine all foreign payees, and whether they are foreign corporations, nonresident aliens, or foreign partnerships.
 - b. Determine all payments of FDAP income to foreign payees.
 - c. Determine any such FDAP income (from step two) that is U.S. sourced and the applicable withholding rate, if any.

Note: Line-by-line review of a withholding certificate (i.e., Form W-8) is necessary to ensure that the form is complete and consistent on its face. Note that a failure on any one line item does not necessarily invalidate the certificate and all claims made therein. However, the examiner should consider such failures carefully and shall take special caution in the case of systemic failures. Note that an invalid certificate may be cured with a valid certificate obtained after the date of the payment provided that certain requirements are met (e.g., affidavit requirement). See Treas. Regs. 1.1441-1(b)(7)(ii) and IRM 4.10.21.9.7.3, Forms W-8 Provided After Date of Payment.

4.10.21.10.3.1
(09-20-2018)
**Determine All Foreign
Payees (Step 1)**

- (1) This first step requires the analysis of the vendor file to identify payees that may be foreign persons. The vendor file is a listing of all payees, including names and other pertinent information relating to the payee. All payees who meet one or more of the following criteria should be a possible foreign payee:
 - a. Payee's EIN starting with 98-xxxxxxx

Note: Only foreign corporations have EINs beginning with 98, and some may begin in 33.)
 - b. Payee's ITIN starting with certain numbering ranges. See IRM 3.13.5.22, Individual Taxpayer Identification Number (ITIN) Format.
 - c. Country: not U.S. or blank
 - d. Zip Code: not U.S. format
 - e. State: not a U.S. state or blank
 - f. City: foreign city
 - g. Vendor number, if coded for foreign payees
 - h. Any other factors which indicate possible foreign status
- (2) The above are recommended indicators to determine that the payee may be foreign. The examiner should review the vendor file to set any other criteria that may be used for the taxpayer.

- (3) Some of the payees selected may be U.S. persons. Therefore, it is recommended that this list of possible foreign payees should be presented to the taxpayer for their review. If the taxpayer can establish that the payee is not foreign, the name should be removed from further review.

4.10.21.10.3.2
(09-20-2018)

**Determine All Payments
of FDAP Income to
Foreign Payees (Step 2)**

- (1) In step two determine which of the payments to foreign payees are payments of FDAP income. Not all payments to the foreign payees selected in step one would be FDAP income. The examiner should consider the facts and circumstances of each taxpayer in determining all possible payments which may result in FDAP income to the foreign person. Some of the most common expenses paid by the taxpayer that may result in FDAP income payments to the foreign payees (both corporations and individuals) are:

- a. Interest
- b. Royalties, patents, copyrights (payments for intellectual assets)
- c. Royalties – natural resources (payments for timber, oil, coal)
- d. Rents
- e. Dividends
- f. Amounts paid to nonresident alien independent contractors for services rendered in the United States
- g. Annuities and pensions paid to nonresident aliens previously employed by the U.S. entity or group
- h. Salaries, wages remuneration paid directly by a U.S. person to its non-resident alien employees, directors

The above is not an all-inclusive list of payments, that may be subject to NRA withholding.

- (2) It is recommended that the examiner should first test the accuracy of how expenses are categorized by the taxpayer before step two is performed. Often expenses are not accurately categorized by the taxpayer. For example, a contract for computer hardware might include a service component, such as training and maintenance services provided by the foreign payee.
- (3) Once the examiner has determined the validity of the categorization, the step two analysis can be performed. The examiner should at least review material payments that may be FDAP even though the taxpayer did not correctly categorize them as such. The examiner should compile all payments of the selected expenses paid to the foreign payees.

4.10.21.10.3.3
(09-20-2018)

**Determine Foreign
Payees FDAP Income
Which Was U.S. Sourced
(Step 3)**

- (1) At this point the examiner has determined payments to foreign payees that are FDAP income. The source of the income (U.S. sourced vs. foreign sourced) should now be determined. See the summary of general sourcing rules from IRC 861, IRC 863, and IRC 865 in Figure 4.10.21-2 below.
- (2) The regulations under Treas. Reg. 1.1441-2(a) require that the income payments be presumed U.S. source when the source is not known to the payer. Therefore, any FDAP income determined in step 2 that the source is unknown to the payer is presumed to be U.S. sourced and subject to a 30% withholding tax. The taxpayer has the burden of proof to overcome the presumption.

Sourcing Rules Type of Income	Determinative Factors (rules may be modified by an applicable treaty)
Personal Services	Generally, where services are performed, subject to potential allocation under Treas. Reg. 1.861-4 and to a limited exclusion based on temporary U.S. presence in IRC 861(a)(3). Even for U.S. source income, withholding under IRC 1441 is not required to the extent the compensation is subject to withholding under IRC 3401 and IRC 3402.
Dividends	Generally, depends on whether paying corporation is domestic or foreign.
Interest	Generally, depends on whether payor is domestic or foreign. Interest paid by a U.S. branch of a foreign corporation is U.S. source income. IRC 884(f)(1)(A). For original issue discount, see IRC 871(g)(3).
Rent	Where the property is located
Royalties - Patents & Copyrights	Where the property is used (benefits derived)
Royalties - Natural Resources	Where the property is located
Pensions	The compensation element (the contribution portion is sourced based on where the related services were performed; the earnings portion is sourced based on the location of the pension trust (e.g., earnings on a U.S. plan are U.S. source income). For allocating between employer contributions and earnings for defined-benefit pension plans, see Rev. Proc. 2004-37. Also reference the income exclusion provided under IRC 871(h) for certain payments from qualified annuity plans under IRC 403(a)(1).

Figure 4.10.21-2

4.10.21.10.4
(09-20-2018)

**Treatment of Personal
Services Paid to Foreign
Persons**

- (1) Payments for personal services often are not subject to NRA withholding. For example, NRA withholding is not required if the compensation is effectively connected with the conduct of a trade or business in the U.S. and is subject to withholding under IRC 3402 (related to withholding on wages). Contact the Foreign Payments Practice Network for information regarding auditing payments for personal services.

4.10.21.10.5
(07-29-2008)

**Suggested Initial
Information Document
Requests (IDR)**

- (1) These information document requests are provided as a guide to the examiner. It is recommended that they be adapted by the examiner to fit the needs of the audit. An example of how some of these requests may be addressed in an IDR is illustrated in Exhibit 4.10.21-5, Sample IDR for Audits of Nonfinancial Services Companies. In general, the topics for this IDR are as follows:
- **Request # 1:** The examiner should request copies of Forms 1042, 1042-S, 5471 and 5472, along with supporting documentation.
 - **Request # 2:** The examiner, with the assistance of the CAS (if available), should inquire about existing systems, policies and procedures used to identify payments subject to NRA withholding for withholding and reporting purposes.

- **Request # 3:** The examiner should inquire about existing systems, policies and procedures used to ensure acquisition of appropriate withholding certificates.
- **Request # 4:** The CAS (if available), with the assistance of the examiner, will attempt to identify the systems along with the specific files or tables to be used as sources of information needed to identify all payments potentially subject to NRA reporting and or withholding.

4.10.21.10.6
(09-20-2018)
**Use of Forms 5471 and
Forms 5472**

- (1) Forms 5471 and 5472 are for reporting transactions between U.S. persons and certain related foreign entities. The examiner should review the transactions which reflect payments by U.S. person to foreign entities to identify payments possibly subject to withholding tax. Using the CAS tool for international information returns, Auditor's Workbench, on electronic Forms 1120 identifies potential U.S. source FDAP payments to affiliates.

4.10.21.10.6.1
(03-23-2023)
Form 5471

- (1) Generally, the Form 5471 is required to be filed by a U.S. person having certain ownership interests in certain foreign corporations. A separate Form 5471 is required to be filed with respect to each foreign corporation meeting these ownership rules. This IRM will focus on the Schedule M attached to the Form 5471. Schedule M is completed by a U.S. person who has controlling interest in a foreign corporation that is a controlled foreign corporation (CFC). See IRC 957. Schedule M reports transactions between the taxpayer and its CFC and reports the following payments made by the taxpayer to the CFC, some of which may be U.S. sourced FDAP income to the CFC:

- a. Compensation received
- b. Commissions received
- c. Rents received
- d. Royalties received
- e. License fees received
- f. Interest received
- g. Dividends received

The examiner should determine if these amounts were subjected to NRA withholding and reported on Forms 1042 and 1042-S. If not, an explanation should be provided by the taxpayer.

4.10.21.10.6.2
(03-23-2023)
Form 5472

- (1) A separate Form 5472 is filed by a corporation with respect to each foreign shareholder owning 25% or more of a U.S. taxpayer. Part IV of the Form reports the following payments by the taxpayer to the foreign corporation, which may be U.S. sourced FDAP income to the foreign corporation:

- a. Compensation / Consideration received
- b. Commissions received
- c. Rents received
- d. Royalties received
- e. Interest received

The examiner should determine if these amounts were subject to NRA withholding and reported on Forms 1042 and 1042-S. If not, an explanation should be provided by the taxpayer.

4.10.21.10.7
(09-20-2018)

Reconciliation of Audit Findings to Forms 1042 and 1042-S

- (1) The examiner should obtain copies of Forms 1042 and Forms 1042-S and compare the audit finding to the gross income reported on the forms. If less than 30 percent was withheld and reported on the filed forms, the examiner should request and examine the Forms W-8 and Forms 8233.

Note: Section 2 of the Form 1042, Reconciliation of Payments of U.S. Source FDAP Income, which is required to be completed by withholding agents starting in 2015, may be a good starting point to reconcile amounts reported on Form 1042 against amounts reported on Form 1042-S.

- (2) If the examiner finds FDAP income and Forms 1042 and 1042-S were not filed, substitute or delinquent return procedures should be followed.

4.10.21.11
(09-20-2018)

Colleges and Universities: Treatment of Scholarships and Grants

- (1) IRC 1441(b) provides that a 14% withholding tax rate generally applies for scholarship and fellowship grants that do not represent compensation for services paid to nonresident aliens who are temporarily present in the United States under an F, J, M, or Q non-immigrant visa classification (but see exception in paragraph (3) for non-degree candidates who do not meet certain requirements). Withholding does not apply to qualified scholarship (under section 117) paid to a candidate for a degree. Scholarship and grants paid to nonresident alien who are not in a F, J, M, or Q nonimmigrant visa status are subject to 30% withholding, unless exempt from tax under a treaty. See Pub 515 for more information.

- a. The compensation portion of a scholarship or grant is generally reportable as wages.
- b. Note that income from scholarship and fellowship grants is not subject to 1099 reporting or backup withholding.

- (2) Since amounts treated as a “qualified scholarship” are excluded from gross income under IRC 117(a), no withholding is required for qualified scholarships paid to a nonresident alien. The 14% tax rate applies to the taxable amounts incident to a qualified scholarship. A qualified scholarship includes the student’s tuition, fees, books, and related expenses, but not living expenses (i.e., room, board or travel).

- (3) In addition, the 14% tax rate applies to grants from a tax-exempt educational or charitable organization, an international organization, the government of a foreign country (or including the states), and an agency of the federal or a state or local government received by a nonresident alien present in the U.S. on an F, J, M, or Q visa even though the individual is not a candidate for a degree at an educational institution. Note that if the grant does not fall within the types described here, the general 30% withholding tax rate applies.

- (4) Withholding at less than the 14% rate may be permitted under certain circumstances to approximate the actual U.S. tax liability of recipients. A student or teacher may submit Form W-4, Employee’s Withholding Allowance Certificate, to the withholding agent to claim personal exemptions and deductions in case of certain taxable payments (e.g., amounts from certain training or exchange programs). Note that the personal exemption has been suspended for tax years 2018 through 2025 under section 11041 of the Tax Cuts and Jobs Act.

- (5) In addition, treaties may exempt scholarship or fellowship income from U.S. tax. This exemption will generally be claimed on a Form W-8BEN. Students, teachers, or researchers claiming an exemption under a treaty are required to

file a Form 8233, Exemption from Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual, with the withholding agent when the individual is also receiving personal services income from the same payor and both types of income are exempt by treaty.

4.10.21.12
(07-29-2008)
Penalties

- (1) The examiner should consider all applicable penalties, including those listed below.
- (2) The Service's approach to penalty administration must ensure consistency, accuracy, impartiality, and representation as stated in IRM 20.1.1.2.2, Fair and Consistent Approach to Penalty Administration. Taxpayers must be given the opportunity to have their interest heard and considered. Examiners need to take an active and objective role in case resolution so that all factors are considered.

4.10.21.12.1
(07-29-2008)
Penalties Applicable to Form 1042 and Related Withholding Tax Deficiencies

- (1) Failure to File – IRC 6651(a)(1)
- (2) Failure to Pay –IRC 6651(a)(2)
- (3) Failure to Deposit – IRC 6656
- (4) Accuracy-Related –IRC 6662
- (5) Fraud – IRC 6663

4.10.21.12.2
(07-29-2008)
Penalties Applicable to Form 1042-S

- (1) Failure to File Correct Information Return – IRC 6721
- (2) Failure to Furnish Correct Information Return – IRC 6722

4.10.21.12.3
(09-20-2018)
Factors to Consider in the Assessment of Penalties

- (1) The examiner must evaluate facts and circumstances in determining when penalties should be assessed. The examiner should consider whether the taxpayer is entitled to any penalty relief. Generally, relief from penalties falls into four separate categories:

- Reasonable cause
- Statutory exception
- Administrative waiver
- Correction of IRS error

IRM 20.1.1.3 should be carefully reviewed and considered before a penalty determination is made. Generally, the taxpayer will have the burden of proof to support their position for non-application of the penalties.

- (2) **Reasonable cause:**
The taxpayer must show why reasonable cause applies. The taxpayer must show why a reasonable person would have failed to properly file, withhold, report or deposit NRA withholding taxes. Ignorance of the law is generally not accepted as reasonable cause.
- (3) Factors which the examiner may consider in determining reasonable cause are as follows:

- a. **Ordinary course of business** – If the withholding, reporting, and depositing of NRA taxes is part of the ordinary course of business of the withholding agent, it may be more difficult for the taxpayer to support a position for nonapplication of a penalty based on reasonable cause.
- b. **Repetitive audit issue** – If the taxpayer was audited on this issue previously and an adjustment was made it will be more difficult for the taxpayer to support their position for nonapplication of a penalty based upon reasonable cause.
- c. **Agreements with the IRS** – The examiner may consider whether the taxpayer has entered into an agreement with the IRS and complied with the remediation plan it submitted to the IRS.
- d. In any case, agents must read IRM 20.1.1.2.3, Managerial Approval for Penalty Assessments, prior to proposing any penalties.

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Exhibit 4.10.21-1 (03-23-2023)**Basic Terms Defined**

Term	Definition
Backup withholding	The withholding required under IRC 3406 with respect to reportable payments made to certain U.S. persons, specifically 24 percent withholding rate on income to a person who has not provided a valid TIN. Note: The rate is 28 percent for payments made prior to January 1, 2018.
Beneficial owner	For withholding purposes, the beneficial owner is the person who, under U.S. tax principles, is required to include the item in gross income on a tax return. See Treas. Reg. 1.1441-1(c)(6)(i). Excluded from this definition are agents of such persons and intermediaries (see definition for Intermediary), as well as certain persons who receive income regarding conduit transactions. See Treas. Reg. 1.1441-7(f).
Change in circumstances	Any change that makes any information on a Form W-8 incorrect (see Withholding Certificate below). The account holder is required to notify the withholding agent within 30 days of such change. In Chapter 3, the Form W-8 becomes invalid when the withholding agent knows or has reason to know of a change in circumstances affecting the correctness of the form. See Treas. Reg. 1.1441-1(e)(4)(ii)(D). Withholding agents have a 90-day grace period for obtaining new documentation on the payee's Chapter 4 status after a change in circumstances.
Chapter 4 status	A person's status as a U.S. person, a specified U.S. person (as defined in Treas. Reg. 1.1473-1(c)), an individual that is a foreign person, a participating FFI, a deemed-compliant FFI, a restricted distributor, an exempt beneficial owner, a nonparticipating FFI, a territory financial institution, an excepted NFFE or a passive NFFE (as defined in Treas. Reg. 1.1471-1(b)(94)).
Disregarded entity	A business entity that has a single owner and is not treated as a corporation under Treas. Reg. 301.7701-2(b). If an entity is disregarded, its owner is treated as the owner of the income for NRA withholding purposes, though different rules may apply for determining a preferential withholding rate under an income tax treaty.
Documentary evidence; other appropriate documentation	The terms "documentary evidence" and "other appropriate documentation" refer to documentation other than a withholding certificate (Form W-8, see Withholding Certificate definition) that may only be provided for documenting the status of payees for payments made outside the United States to offshore obligations (see definition of Offshore Obligations below), or any other evidence that under the IRC or regulations certifies or establishes the status of a payee or beneficial owner as a U.S. or a foreign person. See Treas. Reg. 1.1441-1(c)(17) and 1.1441-1(b)(7).
Documentation	The term "documentation" refers to both withholding certificates and documentary evidence or other appropriate documentation. See Treas. Reg. 1.1441-1(c)(18).

Exhibit 4.10.21-1 (Cont. 1) (03-23-2023)**Basic Terms Defined**

Term	Definition
Effectively connected income (ECI)	Generally, when a foreign person engages in a trade or business within the United States, certain U.S. and foreign source income attributable to such trade or business under the rules of IRC 864(c) will be treated as ECI, which is taxed on a net basis (and reported on a Form 1040NR or 1120F filed by the payee) rather than by withholding at source. To establish a withholding exemption for ECI, the withholding agent must generally receive a beneficial owner's withholding certificate (Form W-8ECI), prior to the payment to the beneficial owner, showing a U.S. TIN and representing under penalties of perjury that the income is effectively connected with the conduct of a trade or business within the United States and that it is includable in the beneficial owner's gross income for the tax year. See Treas. Reg. 1.1441-4(a)(2)(i). But see the presumption rules applicable to certain U.S. branches in the IRC 1441 regulations. FDAP income (defined below) may or may not be effectively connected with a U.S. trade or business. A withholding certificate for a claim for a withholding exemption for ECI is effective only for the item or items of income specified therein.
Exempt recipient	Generally, any payee that is not required to be provided a Form 1099 and is exempt from backup withholding under IRC 3406. Such persons are not necessarily exempt from the NRA withholding requirements.
FATCA withholding	As used in the IRM, the term "FATCA withholding" means withholding on a withholdable payment under FATCA. "FATCA" refers to Chapter 4 of Subtitle A (IRC 1471-1474) of the Internal Revenue Code. A withholding agent must withhold on a payment of U.S. source FDAP income that is a "withholdable payment" (as defined in Treas. Reg. 1.1473-1(a)) to which an exception does not apply under Chapter 4.
Fiscally transparent entity	In connection with obtaining a reduced rate of withholding under a treaty, an entity is treated as fiscally transparent with respect to an item of income to the extent that interest holders in the entity must, on a current basis under relevant foreign law, take into account separately their share of an item of income paid to the entity, whether or not distributed, and must determine the character of the items of income as if they were realized directly from the sources that paid it to the entity. For example, partnerships, common trust funds, and certain trusts may be generally considered to be fiscally transparent with respect to items of income received by them. Such entities are not considered to have derived income for purposes of IRC Section 894(c), and they may be ineligible for treaty benefits under this code section, though their interest holders may be so eligible.

Exhibit 4.10.21-1 (Cont. 2) (03-23-2023)**Basic Terms Defined**

Term	Definition
Fixed, Determinable, Annual or Periodical (FDAP) Income	In general, income that is includible in gross income under IRC Section 61. Income is fixed when it is paid in amounts known ahead of the time paid. Income is determinable whenever there is a basis for calculating the amount to be paid. Examples of FDAP income include interest, dividends, rents, royalties, and compensation. See Treas. Reg. 1.1441-2. Certain U.S. source FDAP income is excluded from withholding, such as interest qualifying under IRC Sections 871 or 881 as portfolio interest (see definition below) and income excludible under a U.S. income tax treaty with a country with respect to which the foreign recipient meets the residency and other requirements for obtaining the treaty exemption. These exceptions are for Chapter 3 purposes only. See also IRC Section 894(c). Gains from asset sales are generally not FDAP income. But see the withholding requirement applicable to sales of U.S. real estate or stock in a U.S. real property holding company. See Treas. Reg. 1.1445-1(b).
Foreign corporation	Any corporation that is not a domestic corporation. See IRC 7701(a)(5). A domestic corporation is one that was created or organized in the U.S. or under laws of the U.S. or any of its states, or the District of Columbia. See Treas. Reg. 1.1441-1(c)(4).
Foreign central bank of issue	A bank that is by law or government sanction the principal authority, other than the government itself, to issue instruments intended to circulate as currency. Such a bank is generally the custodian of the banking reserves of the country under whose law it is organized. For purposes of IRC 895, the Bank of International Settlements is treated as though it were a foreign central bank of issue. IRC 895 generally exempts from U.S. taxation income that a foreign central bank of issue receives from obligations of the United States (or of any agency or instrumentality thereof) or from interest on deposits with persons carrying on the banking business unless such obligations or deposits are associated with commercial banking functions or other commercial activities of the foreign central bank of issue. An exemption might also apply under IRC 892 for foreign central banks not engaged in commercial activities within the U.S. A foreign central bank of issue should generally provide a Form W-8EXP to a withholding agent to establish eligibility for an applicable withholding exemption under those sections. Foreign central banks of issue are exempt beneficial owners under Chapter 4.
Foreign financial institution (FFI)	For Chapter 4 purposes, a "foreign financial institution" is any financial institution (as defined in IRC 1471(d)(5)) that is a foreign entity. See also Treas. Reg. 1.1471-5(d). This shall not include a financial institution which is organized under the laws of any possession of the United States. The term FFI also includes a foreign branch of a U.S. financial institution with a QI agreement in effect.

Exhibit 4.10.21-1 (Cont. 3) (03-23-2023)**Basic Terms Defined**

Term	Definition
Foreign flow-through entity	A foreign flow-through entity is a foreign partnership, a foreign simple trust, foreign grantor trust or, for payments for which a reduced rate of withholding is claimed under an income tax treaty, any entity to the extent it is considered fiscally transparent (as defined above). In such cases, withholding is determined based on the status of the entity's owners for Chapter 3 purposes only. See definition of Beneficial Owner. When an entity executes an applicable withholding agreement with the IRS to act as either a Withholding Foreign Partnership or Trust, it is then itself generally authorized to act as a withholding agent with respect to certain of its owners under Chapter 3 and Chapter 4 only. See Rev. Proc. 2017-21 and subsequent amendments to the Withholding Foreign Partnership and Withholding Foreign Trusts agreement. Foreign estates and foreign complex trusts are not generally considered flow-through entities for withholding purposes. Whether an entity is a partnership is determined under the entity classification regulations. See Treas. Reg. 1.1441-1(c)(27) for the definition of partnership. In Chapter 4, a foreign flow-through entity is the payee with respect to a payment only, if the flow-through entity is : (1) an FFI that is not a participating FFI or a deemed-compliant FFI, or restricted distributor receiving a payment of U.S. source FDAP income, (2) an excepted NFFE that is not acting as an agent or intermediary with respect to the payment, (3) a WP or WT that is not acting as an agent or intermediary with respect to payment, or (4) receiving income that is (or is deemed to be) ECI or receiving a payment of gross proceeds from the sale of property that can produce ECI and that is excluded from the definition of a withholdable payment. See Treas. Reg. 1.1471-3(a)(3)(ii)(A).
Foreign government exemption	Regarding the withholding exemption under Treas. Reg. 1.1441-8, a foreign government includes only its integral parts or controlled entities as defined in Treas. Reg. 1.892-2T. Only a foreign government or an international organization (defined below) qualifies for exemption from taxation under IRC 892. This section generally excludes from gross income and exempts from U.S. taxation income which a foreign government receives from investments in the United States in stocks, bonds or other domestic securities; financial instruments held in the execution of governmental financial or monetary policy; and interest on deposits in banks in the United States of monies belonging to the foreign government. Income of a foreign government from any of these other sources listed below are not exempt from taxation: (a) that derived from the conduct of commercial activity, (b) that received directly or indirectly from a controlled commercial entity, and (c) that derived from the disposition of any interest in a commercial entity. Foreign governments are exempt beneficial owners for certain payments under Chapter 4.
Foreign grantor trust	A foreign trust all or a portion of which is treated as owned by the grantor or other person under IRC 671 through IRC 679.
Foreign person	Any person who is not a U.S. person including a QI branch of a U.S. financial institution. See Treas. Reg. 1.1441-1(c)(2). Nonresident alien withholding tax applies only to foreign persons.

Exhibit 4.10.21-1 (Cont. 4) (03-23-2023)**Basic Terms Defined**

Term	Definition
Hybrid entity	For treaty purposes, a hybrid entity is an entity that is treated as fiscally transparent in one jurisdiction, but not another (see definition for Fiscally Transparent Entity). A domestic hybrid entity is a U.S. entity that is fiscally transparent for U.S. tax purposes, but not fiscally transparent for foreign tax purposes. A foreign hybrid entity is a foreign entity that is fiscally transparent for U.S. tax purposes, but not fiscally transparent for foreign tax purposes. Hybrid entity status is relevant regarding both treaty benefits and for determining the beneficial owner of income under U.S. tax principles.
Intermediary	Any person that acts as a custodian, broker, nominee, or agent for another person, regardless of whether that other person is the beneficial owner of the amount paid.
International organization	An international organization is any public international organization entitled to enjoy privileges, exemptions, and immunities as an international organization under the International Organizations Immunities Act (22 USC 288). In general, to qualify as an international organization, the U.S. must participate in the organization pursuant to a treaty or under the authority of an Act of Congress authorizing such participation. See Treas. Reg. 1.1441-8 concerning the related exemption from NRA withholding.
Non-financial foreign entity (NFFE)	For Chapter 4 purposes, a nonfinancial foreign entity (or NFFE) is a foreign entity that is not a financial institution (as defined in IRC 1471(d)(5)). See also Treas. Reg. 1.1471-1(b)(80).
Nonparticipating FFI	For Chapter 4 purposes, a nonparticipating FFI (or NPFFI) is an FFI other than a participating FFI, a deemed-compliant FFI or an exempt beneficial owner under Treas. Reg. 1.1471-1(b)(82).
Nonqualified intermediary	Any intermediary that is not a U.S. person and that is not a qualified intermediary. See definitions for Intermediary and Qualified Intermediary.
Nonresident alien individual	Any individual who is not a U.S. citizen or resident alien of the U.S. See IRC 7701(b).
NRA Withholding	As used in this IRM, the term “NRA withholding” refers to withholding under sections 1441-1443 of Chapter 3 of the Internal Revenue Code. In general, certain reportable amounts (see definition of Reportable Amounts) paid to foreign persons from sources within the U.S. that are fixed or determinable annual or periodical (FDAP) income and that are not reported as effectively connected with a U.S. trade or business are subject to NRA withholding. Withholding applies to limited types of gain income not related to real estate interests, including gains from dispositions of natural resources under IRC 631 and gains from contingent payments received from the sale or exchange of certain intangible property. See also FDAP income definition. An amount is considered paid when it is includable in income under the cash basis method of accounting. A payment is subject to withholding whether it is made directly to the beneficial owner or made for the benefit of the beneficial owner, including a payment to that person’s creditors. A payment for withholding purposes may also arise based on an allocation of income under IRC 482. See Treas. Reg. 1.1441-2(e).

Exhibit 4.10.21-1 (Cont. 5) (03-23-2023)**Basic Terms Defined**

Term	Definition
Offshore obligations	The term “offshore obligation” means an offshore obligation defined in 1.6049-5(c)(1) by substituting the terms “withholding agent” or “financial institution” for the term “payor”). See Treas. Reg. 1.1471-1(b)(88). Determining the existence of an offshore obligation is potentially relevant regarding the presumption rules (as defined below) for determining the status of certain undocumented payees and regarding the use of documentary evidence in lieu of a withholding certificate (both as defined herein). These are in general accounts which are located outside the U.S. See Treas. Reg. 1.6049-5(c)(1) for more on the rules applicable to offshore obligations.
Over-withholding adjustments	<p>If the withholding agent discovers before the due date for filing Form 1042-S that it over-withheld NRA or Chapter 4 withholding tax in the tax year following the calendar year of withholding, it can use either the reimbursement or the set-off procedure to adjust the over-withholding.</p> <p>a. Reimbursement procedure – Under this procedure, the withholding agent repays the payee with its own funds by the due date for filing Form 1042-S and reports for the year of the overpayment (1) the repaid amount on a timely filed Form 1042-S to the payee and (2) a claim for credit on Form 1042. The withholding agent is then reimbursed by reducing any subsequent deposits it makes before the end of the following year with respect to payments subject to withholding.</p> <p>b. Set-off procedure – Under this procedure, the withholding agent repays the payee by reducing the amount it would have been required to withhold on later payments it makes to the same person by the earlier of the due date or actual filing date of Form 1042-S. See Treas. Reg. 1.1461-2 and 1.1474-2(a).</p>
Portfolio interest	<p>Portfolio interest is generally excluded as an amount subject to NRA withholding, though it is generally subject to Forms 1042/1042-S reporting.</p> <p>Note: Portfolio interest is still subject to withholding under Chapter 4.</p>
Presumption rules	Rules for determining an undocumented account holder’s / payee’s (as defined below) relevant characterizations for withholding purposes, such as whether an entity is a U.S. or foreign person. See Treas. Reg. 1.1441-1(b)(3). These rules may sometimes be superseded by a withholding agent’s actual knowledge concerning the payee. See definitions for Reason to Know and Standard of Knowledge below.
Qualified intermediary	<p>A person that is a party to a withholding agreement with the IRS and is:</p> <p>a. A foreign financial institution or a foreign clearing organization (other than a U.S. branch or U.S. office of the institution or organization) that has a specified Chapter 4 status;</p> <p>b. A foreign branch or office of a U.S. financial institution or a foreign branch or office of a U.S. clearing organization;</p> <p>c. A qualified derivatives dealer that is an eligible entity;</p> <p>d. Any other person the IRS accepts as a qualified intermediary. See Rev. Proc. 2017-15 and any amendments thereto. See Treas. Reg. 1.1441-1(e)(5)(ii) and (e)(6).</p>

Exhibit 4.10.21-1 (Cont. 6) (03-23-2023)**Basic Terms Defined**

Term	Definition
Reason to know	A standard of knowledge that might result in a requirement for a withholding agent to withhold at a rate more than that which would result from reliance on a payee's withholding certificate or from applying the presumption rules (defined above). See Treas. Reg. 1.1441-7(b)(2-3), 1.1441-1(b)(3)(ix)(B). See also "Standard of Knowledge" definition.
Reportable amounts	In general, the term "reportable amount" means an amount subject to withholding within the meaning of Treas. Reg. 1.1441-2(a), bank deposit interest (including original issue discount) and similar types of deposit interest described in IRC 871(i)(2)(A) or 881(d) that are from sources within the United States, and any amount of interest or original issue discount from sources within the United States on the redemption of certain short-term obligations described in IRC 871(g)(1)(B) or 881(e). See Treas. Reg. 1.1441-1(e)(3)(vi).
Reportable payments	Payments made to certain U.S. recipients that are required to be shown on a return required under IRC 6041 - 6050 and for which withholding may be required under the conditions prescribed by IRC 3406.
Resident alien	An alien individual who meets the green card test or the substantial presence test or makes a first year election for the calendar year. See IRC 7701(b).
Reverse hybrid entity	Any entity that is not fiscally transparent under U.S. tax law principles (i.e., is treated as a corporation), but that is fiscally transparent under the laws of a jurisdiction with which the U.S. has an income tax treaty (such as an entity like a partnership)
Standard of knowledge	Treas. Reg. 1.1441-7(b) defines the standards the withholding the agent must apply to determine the correct withholding and reporting requirements under IRC 1441 - 1443.
Tax liability for failure to withhold	The withholding agent will be liable for a tax amount resulting from failing to withhold or deposit amounts subject to NRA withholding. See IRC 1461. Both the withholding agent and the foreign recipient may be held liable for such tax, applicable interest and any penalties resulting from a failure to withhold.
U.S. Person	Under IRC 7701(a)(30), the term "United States person" means –(A) a citizen or resident of the United States, (B) a domestic partnership, (C) a domestic corporation, (D) any estate (other than a foreign estate, within the meaning of paragraph (31)) and (E) any trust if – (i) a court within the United States can exercise primary supervision over the administration of the trust, and (ii) one or more United States persons have the authority to control all substantial decisions of the trust.
U.S. sourced income	In general, the source of income is the place where income-generating activity occurs or where the asset giving rise to the relevant income is located. IRC Sections 861, 863 and 865 prescribe rules for determining when certain types of income are U.S. or foreign sourced, which is relevant for nonresident alien withholding. See definition of NRA Withholding and Figure 4.10.21-2 for a summary of sourcing rules.

Exhibit 4.10.21-1 (Cont. 7) (03-23-2023)**Basic Terms Defined**

Term	Definition
U.S. withholding agent	A U.S. person who has control, receipt, custody, disposal or payment of income to a foreign person.
Withholdable payment	Generally, the term “withholdable payment”, means a payment of U.S. source fixed or determinable annual or periodical (FDAP) income for Chapter 4 purposes. The term “withholdable payment” does not include income connected with a U.S. trade or business that is taken into account under IRC 871(b)(1) or IRC 882(a)(1) for the taxable year.
Withholding certificate	The term “withholding certificate”, per Treas. Reg. 1.1441-1(c)(16), means various versions of Form W-8, Form 8233, Form W-9 (Form W-9 indicates U.S. status), or any other certificate that under the IRC or regulations certifies or establishes the status of a payee for withholding or reporting purposes. This term is referred to alternatively in this section as either a withholding certificate or as a Form W-8. See IRM 4.10.21.6.2 and Exhibit 4.10.21-2 for descriptions of the different types of Forms W-8 and other forms.
Withholding foreign partnership or withholding foreign trust	A foreign partnership or a foreign simple or grantor trust that has entered into a withholding agreement with the IRS in which it agrees to assume primary withholding responsibilities under Chapters 3 and 4 with respect to certain of its partners, beneficiaries or owners. See Treas. Regs. 1.1461-1(c)(1)(ii)(A)(3), 1.1441-5(c)(2) and 1.1441-5(e)(5)(v).
Withholding agent	U.S. or foreign person, in whatever capacity acting, that has control, receipt, custody, disposal or payment of an amount subject to Chapter 3 withholding. A withholding agent may be an individual, corporation, partnership, trust, association, nominee (under IRC 1446), or any other entity, including any foreign intermediary, foreign partnership, or U.S. branch of certain foreign banks and insurance companies. Generally, the person who pays (or causes to be paid) the amount subject to withholding to the foreign person (or to its agent) must withhold. See Treas. Reg. 1.1441-7. For the purposes of Chapter 4, a withholding agent is a U.S. or foreign person, in whatever capacity acting, that has control, receipt, custody, disposal, or payment of a withholdable payment. See Treas. Reg. 1.1473-1(d).
Withholding statement	The written statement provided to a withholding agent by an intermediary or by a nonwithholding partnership or trust for allocating payments and for applying withholding to each underlying account holder or owner. The statement must contain sufficient information for a withholding agent to apply the correct rate of withholding on payments for the accounts identified on the statement and to properly report such payments on Forms 1042-S and Forms 1099, as applicable.

Exhibit 4.10.21-2 (03-23-2023)**Types of Withholding Certificates**

Form	Description
Form W-8 BEN (Feb. 2006 version)	The title of the form is “Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding”, which may be used for claims of treaty benefits by foreign persons. Note: This form was used by both foreign individuals and foreign entities prior to 2014 when the form was revised and two forms were created: W-8BEN (Individuals) and W-8BEN-E (Entities). The 2006 version of Form W-8BEN was in effect for foreign entities until December 31, 2014. Withholding agents that obtained the 2006 version of the Form W-8BEN prior to January 1, 2015 can rely on that form, for Chapter 3 purposes, until the form expires (based on validity period rules).
Form W-8 BEN	Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Individuals)
Form W-8 BEN-E	Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities)
Form W-8 ECI	Certificate of Foreign Person’s Claim That Income is Effectively Connected with the Conduct of a Trade or Business in the United States
Form W-8 EXP	Certificate of Foreign Government or Other Foreign Organization for United States Tax Withholding and Reporting
Form W-8 IMY	Certificate of Foreign Intermediary, Foreign Flow-Through Entity, or Certain U.S. Branches for United States Tax Withholding and Reporting
Form 8233	Exemption from Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual
Form W-9	Request for Taxpayer Identification Number and Certification

Exhibit 4.10.21-3 (09-20-2018)**New Account Examination Procedures**

The examiner should review the procedures for new accounts using the following criteria:

- a. Any information, other than withholding certificates (i.e., Forms W-9 and W-8), used to determine if the account is held by a U.S. person or a foreign person, such as:
 - Residence and mailing addresses shown on account opening applications
 - Documentation submitted by the account holder for identification purposes (i.e. passports, driver's license, articles of incorporation, etc.)
 - Account-file information or correspondence
- b. Procedures used to determine an account holder's status for withholding purposes, including when the account is not documented with a withholding certificate or when information provided during account opening is inconsistent with the information showing on the certificate. The examiner should further determine if the information noted in part (a) above is used for withholding purposes in lieu of the presumption rules for undocumented account holders.

Note: The information noted in parts (a) and (b) cannot be used in lieu of presumption rules for undocumented account holders. The U.S. withholding agent can rely on a valid withholding certificate (i.e. Form W-8), documentary evidence only in the case of payments made outside the U.S. with respect to offshore obligations, or the regulations' presumption rules to determine the status of a payee. This information is relevant, however, because if for a specific account holder the information contradicts claims on a withholding certificate or documentary evidence, such documents may be unreliable or invalid based on the applicable standard of knowledge imputed to the withholding agent (see Standard of Knowledge definition above). See also "Requirement to Rely on Presumption Rules" and "Validation Process" sections.

- c. Procedures which require the separation of functions, if applicable.
- d. Procedures for recording and updating information into the withholding and account systems (i.e., master files) to reflect information received via Forms W-8 and opening procedures. At a minimum, the following information should be captured by the nonresident alien withholding and accounting systems :
 - Foreign/U.S. status
 - Chapter 3 status
 - Chapter 4 status
 - Type of Form W-8 (BEN, BEN-E, EXP, IMY, or ECI), Form 8233 or Form W-9, used to document the account holder
 - Type of entity (corporation, trust, etc.)
 - Treaty claim (Part II of Form W-8BEN; Part III of Form W-8BEN-E) and limitations or conditions set forth on this form
 - Expiration date of Form W-8 (if applicable)

Exhibit 4.10.21-4 (03-23-2023)

Sample IDR for Audits of Financial Services Companies

Form 4564	Department of the Treasury Internal Revenue Service Information Document Request	Request Number
To: (Name of Taxpayer and Company, Division or Branch)		Subject: NRA Withholding Taxes
IDR OF FINANCIAL INSTITUTION - NRA WITHHOLDING AGENT		Submitted to: Dates of Previous Requests:
Description of Documents Requested: [For all documents, electronic documents are required when the original is electronic. Word and Excel are required rather than pdf when available.]		
Please provide the following:		
1a) Forms 1042 and Forms 1042-S for calendar years _____, _____, & _____. [For paper-filed Forms 1042-S, provide a computer readable Excel version of the filings. For electronically filed Forms 1042-S, provide FIRE system files submitted.]		
1b) Work papers and other supporting documentation used in the preparation of Forms 1042 & 1042-S requested above.		
1c) Listing of names and departments of those persons who had primary responsibility for the preparation of Forms 1042 & 1042-S.		
2a) All internal audit reports, for the years shown in 1a above, that pertain to each company's fiduciary activities, including but not limited to:		
	i) customer account openings	
	ii) documentation validation (U.S. vs. Foreign status, Entity type, etc.)	
	iii) renewal of expiring or invalid Forms W-8	
	iv) recording of transactions of the fiduciary accounts	
	v) determination of source (U.S. vs. Foreign)	
	vi) type of income (dividend vs. interest)	
	vii) application of withholding and reporting	
2b) All operating manuals and written procedures for the years shown in 1a above, that pertain to each entity's fiduciary activities, including but not limited to:		
	i) customer account openings	
	ii) documentation validation (U.S. vs. Foreign status, Entity type, etc.)	
	iii) renewal of expiring or invalid Forms W-8	
	iv) recording of transactions of the fiduciary accounts	
	v) determination of source (U.S. vs. Foreign)	
	vi) type of income (dividend vs. interest)	
	vii) application of withholding and reporting	
2c) Names, Titles and Departments of those persons who had primary responsibility for functions indicated in 2a & 2b.		
3a) Is Securities Lending conducted out of your bank? If so, please provide written explanation of the nature of this business.		
3b) Is Loan Syndication conducted out of your bank? If so, please provide written explanation of the nature of this business.		

Exhibit 4.10.21-5 (03-23-2023)**Sample IDR for Audits of Nonfinancial Services Companies**

Form 4564	Department of the Treasury Internal Revenue Service Information Document Request	Request Number
To: (Name of Taxpayer and Company, Division or Branch)	Subject: NRA Withholding Taxes	
IDR OF NONFINANCIAL INSTITUTION - NRA WITHHOLDING AGENT	Submitted to: Dates of Previous Requests:	
Description of Documents Requested: [For all documents, electronic documents are required when the original is electronic. Word and Excel are required rather than pdf when available.]		
Please provide the following:		
1a) Forms 1042, Forms 1042-S, Forms 5471 and Forms 5472 for each entity of the consolidated group for the calendar years _____, _____, & _____. [For paper filed forms 1042-S provide a computer readable Excel version of the filings. For electronically filed forms 1042-S, provide FIRE system files submitted.]		
1b) Work papers and other supporting documentation used in the preparation of the above requested forms.		
1c) Any internal audit reports for the years identified in item 1a above that pertain to each company's withholding and reporting obligations, including but not limited to identification of relevant payments, validation procedures and procedures for reporting.		
1d) Operation manuals and written procedures in effect for the years identified in item 1a above pertaining to each company's withholding and reporting obligations, including but not limited to identification of relevant payments, validation procedures and procedures for reporting.		
1e) Names, titles and departments of those persons who had primary responsibility for the preparation of Forms 1042, 1042-S, 5471, and 5472.		
1f) Names, titles and departments of those persons who are familiar with the documents mentioned in items 1c and 1d and persons that had primary responsibility for the functions mentioned in items 1c and 1d.		
To the extent your operations manuals or written procedures in effect for the years identified in 1a do not answer, please provide the following information:		
2a) Please identify the systems, and provide operating manuals and written procedures that ensure that all payments made to non-U.S. persons (individuals or entities) that are subject to NRA withholding (Treas. Reg. 1.1441 – 1.1446) have been identified.		
2b) Please indicate your procedures to determine whether a payment is:		
	i) made to a foreign person	
	ii) fixed or determinable annual or periodical (FDAP)	
	iii) U.S. sourced	
2c) Please provide a list of all departments that make payments to all foreign individuals and/or entities. Please note the term payments includes, but is not limited to:		
	i) payments to foreign vendors	
	ii) payments of Investment Income to foreign persons	
	iii) payments to foreign related parties	
	iv) payments of pension benefits to foreign persons	
2d) Please indicate names and titles of persons who have primary responsibility for any department identified in your response to question 2c.		
3) Please identify the systems, and provide operating manuals and written procedures that ensure withholding certificates (Forms W-8 or Forms 8233) are requested from foreign individuals and / or entities receiving income subject to NRA withholding.		

Exhibit 4.10.21-6 (03-23-2023)**Validity Period of Form W-8 – Treas. Regs. 1.1441-1(e)(4)(ii)**

Notwithstanding the validity periods permitted by paragraphs (c)(6)(ii)(A) through (D) of this section, a withholding certificate, Written statement, and documentary evidence will cease to be valid if the withholding agent has knowledge or a change in circumstances that makes the information on the documentation incorrect. Therefore, a withholding agent is required to institute procedures to ensure that any change to the customer master files that constitutes a change in circumstances described in paragraph (c)(6)(ii)(E) of this section is identified by the withholding agent. In addition, a withholding agent is required to notify any person providing documentation of the person's obligation to notify the withholding agent of a change in circumstances.

Form Type	Expires
W-8BEN	<p>A Form W-8BEN generally will remain in effect for the period starting the date the form was signed and ending December 31 of the third succeeding calendar year, unless there is a change in circumstances that makes the information on the form no longer accurate. For example, a Form W-8BEN signed September 2019 will expire 12/31/2022.</p> <p>A Form W-8BEN, except for the section of the form that includes the claim for treaty benefits, will remain valid until there is a change in circumstances that makes the form no longer accurate, provided that:</p> <ul style="list-style-type: none"> • The Form W-8BEN and documentary evidence supporting individual's claim of foreign status are provided together (treated as provided together if they are provided within 30 days of each other). • The withholding agent does not have a current U.S. residence or mailing address for the payee, does not have one or more current U.S. telephone numbers that are the only telephone numbers the withholding agent has for the payee, and for payments described in Treas. Reg. 1.6049-5(c)(1), the withholding agent has not been provided standing instructions to make a payment to an account in the U.S. for the obligation. <p>Note that the portion of the Form W-8BEN that includes the treaty claim is subject to the general 3-year validity rule. The general rule is that documentation becomes invalid on the date that the withholding agent holding the certificate or documentation knows or has reason to know that there is a change in circumstances.</p>
W-8-BEN-E	<p>A Form W-8BEN-E generally will remain in effect for the period starting the date the form was signed and ending December 31 of the third succeeding calendar year, unless there is a change in circumstances that makes the information on the form no longer accurate. For example, a Form W-8BEN-E signed September 2019 will expire 12/31/2022).</p> <p>A Form W-8BEN-E, except for the section of the form that includes the claim for treaty benefits, will remain valid until there is a change in circumstances that makes the form no longer accurate, provided that:</p> <ul style="list-style-type: none"> • The Form W-8BEN-E and documentary evidence supporting entity's claim of foreign status are provided together (treated as provided together if both are received by the withholding agent before the validity period of either the withholding certificate or the documentary evidence would otherwise expire under the general validity rules). <p>Note that the portion of the Form W-8BEN-E that includes the treaty claim is subject to the general 3-year validity rule.</p>

Exhibit 4.10.21-6 (Cont. 1) (03-23-2023)**Validity Period of Form W-8 – Treas. Regs. 1.1441-1(e)(4)(ii)**

Form Type	Expires
W-8ECI	A Form W-8ECI will remain in effect for the period starting the date the form was signed and ending December of the third succeeding year, unless there is a change in circumstances that makes the information on the form no longer accurate. For example, a Form W-8ECI signed September 2019 will expire 12/31/2022. See Treas. Reg. 1.1441-1(e)(4)(ii)(C) and 1.1471-3(c)(6)(ii)(D).
W-8EXP	<p>Generally, a W-8EXP will remain in effect for the period starting the date the form was signed and ending December 31 of the third succeeding calendar year, unless there is a change in circumstances that makes the information on the form no longer accurate. For example, a Form W-8EXP signed September 2019 will expire 12/31/2022).</p> <p>A Form W-8EXP provided by an entity claiming tax exempt status under section 501(c) that is NOT a private foundation (under IRC 509), will remain valid until there is a change in circumstances that makes the form no longer accurate, provided that the withholding agent reports on Form 1042-S at least one payment annually to the entity.</p> <p>A Form W-8EXP provided by a foreign government (or a person representing to be an integral part of a foreign government), a foreign central bank of issue or the Bank for International Settlements, will remain in effect until a change in circumstances makes any information on the form incorrect.</p>
W-8IMY	Generally, a Form W-8IMY will remain in effect until circumstances change that make the information on the certificate no longer correct. The indefinite validity period, however, does not extend to any withholding certificate, documentary evidence, or withholding statements associated with the certificate.

Documentary evidence will generally remain in effect for the period starting the date the documentation was provided to the withholding agent and ending December 31 of the third succeeding calendar year. Documentary evidence provided to establish a payee's foreign status will remain in effect for the period starting the date the documentation was provided to the withholding agent and ending December 31 of the third succeeding calendar year. However, if the documentary evidence has an expiration date, it may be treated as valid until that expiration date if doing so will provide a longer validity period than the 3-year period. Documentary evidence that is generally not renewed or amended (e.g., certificate of incorporation) will remain valid indefinitely.

If a **change in circumstances** makes any information on the Form W-8 which was previously submitted incorrect, the account holder must notify the withholding agent within 30 days of the change in circumstances and a new Form W-8 will be required. Note that for purposes of Chapter 3, a person is considered to have a change in circumstances only if such change affects the person's claim of Chapter 3 status.