

New Federal Tax Withholding Rules for Nonresident Aliens

Service Request 81561

University of California
Office of the President
Payroll Coordination & Tax Services
June 28, 2006
Revised January 25, 2007

SR 81561 Federal tax withholding changes for nonresident aliens

Objective:

The service request addresses requirements to change the Payroll/Personnel System (PPS) to conform to new Internal Revenue Service regulations regarding the calculation of Federal Withholding Tax for certain nonresident aliens.

Project Type:

This is an upgrade to the Payroll/Personnel System (PPS).

Requested by:

Payroll Coordination and Tax Services in response to Internal Revenue Service notice 2005-76.

Analyst:

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Due Date(s):

These changes are Date Mandated. The changes must be implemented after check dates in December 2006 but before any check dated in January 2007.

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I. Background

The Internal Revenue Service (IRS) issued new rules (Notice 2005-76) for determining the amount of Federal withholding tax employers must withhold from salaries and wages paid to nonresident alien (NRA) employees employed in the United States. Because certain NRA employees were experiencing over withholding of income tax on their wages for services performed within the United States, the IRS reconsidered the requirements for determining the amount of income tax to be withheld under section 3402 from the wages of nonresident alien employees. These new rules are designed to provide for withholding on the wages of a NRA employee that more closely approximates the income tax liability of the NRA. The changes also include new rules for NRA employees in completing Form W-4, Employee's Withholding Allowance Certificate.

II. Effective Date

The rules are effective with respect to wages paid on or after January 1, 2006. However, with respect to wages paid prior to January 1, 2007, the IRS will not assert any penalties related to any under withholding caused by the transitioning to the new rules.

III. Current Procedures

Currently, NRA employees may only claim "Single" marital status (regardless of actual marital status) and may generally only claim "0" (zero) or "1" (one) withholding allowance. Please note that NRAs from Canada, Mexico, and South Korea may claim more than one withholding allowance. After subtracting the value of one personal allowance (if claimed), the balance would be taxed using the IRS Table for Percentage Method of Withholding. NRAs have an additional amount of NRA Federal tax withheld from their pay based on their payroll period. Because NRAs are not permitted to claim the standard deduction, the additional NRA tax was to offset the standard deduction built into the withholding tables.

The Payroll/Personnel System (PPS) automatically establishes the deduction GTN 301 on the EDB record for NRAs with a Citizenship Status Code (EDB 0109) value of "N" or "A". The NRA rate of taxes currently withheld is as follows:

\$15.30 - Bi-weekly
\$16.60 - Semi-Monthly
\$33.10 - Monthly

IV. New Procedures

- The PPS needs to be modified to NOT establish an amount in GTN 301 for the additional NRA tax.
- The Federal withholding tax (FWT) deduction for NRA employee's with Citizenship Status Code of "N" or "A" should be calculated by taking the employee's Federal Taxable Gross from the compute, adding a fixed amount to that value, and using the result to look up the tax in the Federal Tax Table. The amount¹ to be added to the gross is based on the pay cycle being run:

\$ 102.00 – Biweekly
\$ 110.00 – Semi -Monthly
\$ 221.00 – Monthly

This amount must not be included in the employee's Federal taxable gross; it is used solely for purposes of calculating the FWT deduction amount.

This amount must not be included on Form W-2, Wage and Tax Statement or the Form 1042-S, Foreign Person's U.S. Source Income Subject to Withholding as it does not represent an actual increase to the employee's wages but is used solely for calculation of the FWT deduction.

- The procedures require that NRAs complete a new Form W-4. Campuses are required to request a new W-4 form from these employees.
- NRA postdoctoral scholars (title code 3253 and 3254) will continue to be taxed at either 14 % or 30% rate.
- Please note that NRA employees must continue to claim "Single" marital status (regardless of actual marital status) and may generally only claim "0" (zero) or "1" (one) withholding allowance.
- These changes do not affect State of California income tax.

¹ Please note that amounts also exist for employees paid daily, weekly, quarterly, semiannually, and annually. However, the University does not use amounts associated with these pay cycles.

V. Requested Changes

The new procedures will require updates to several Control Tables and programming changes to do the calculation of the NRA tax. These changes include modifications to the Gross-to-Net Table, System Messages Table, System Parameters Table, Online EDB screens, Web EDB Tax screen, EDB Maintenance process, and compute process.

A new procedure should be developed to add an amount to the Federal taxable gross of certain NRA employees for purposes of calculating the Federal income tax deduction for each payroll period. The specific amount to add depends on the payroll period bi-weekly, semi-monthly, or monthly.

VI. Control Tables

Gross-to-Net Table (GTN)

The GTN Table should be modified to inactivate the following GTN number established for additional NRA tax:

<u>GTN Number</u>	<u>Description</u>
301	NRA Tax

System Messages Table

Since the NRA additional Federal tax will no longer be taken messages associated with the additional tax are no longer needed. The System Message Table should be updated to remove the following messages:

00-935 ENTRY FOR GTN 301 NRA TAX NOT ON GTN TABLE

08-219 ADDITIONAL NONRES ALIEN TAX NOT REQUIRED: WILL BE SET TO BLANK

12-199 ADDITIONAL NONRES ALIEN TAX NOT REQUIRED: HAS BEEN SET TO BLANK

08-222 ADDITIONAL NONRESIDENT ALIEN TAX WILL BE ESTABLISHED

12-200 ADDITIONAL NONRESIDENT ALIEN TAX HAS BEEN SET

System Parameter Table

The System Parameter Table parameter number 74 (NRA FED TAX) carries the additional Federal income tax that is added to the records of NRA employees with a Citizenship Status Code value "N" or "A". The new procedures require that we no longer add an additional amount to the records of NRAs. The additional amounts are listed below:

\$15.30 - Bi-weekly
\$16.60 - Semi-Monthly
\$33.10 - Monthly

The System Parameter # 74 should be returned to base and marked "Reserved - Base".

VII. EDB Maintenance

- The EDB maintenance process should be modified to remove edits that are associated with the following system messages:

00-935 ENTRY FOR GTN 301 NRA TAX NOT ON GTN TABLE
08-219 ADDITIONAL NONRES ALIEN TAX NOT REQUIRED: WILL BE SET TO BLANK
12-199 ADDITIONAL NONRES ALIEN TAX NOT REQUIRED: HAS BEEN SET TO BLANK
08-222 ADDITIONAL NONRESIDENT ALIEN TAX WILL BE ESTABLISHED
12-200 ADDITIONAL NONRESIDENT ALIEN TAX HAS BEEN SET

- The EDB Maintenance process needs to be modified to NOT establish an amount for GTN 301, the additional NRA tax.
- The EDB Periodic Monthly Maintenance process needs to be modified to NOT establish an amount for GTN 301, the additional NRA tax.
- The calendar year-end process also needs to be modified to NOT establish an amount for GTN 301, the additional NRA tax.

VIII. Payroll Compute

- During the compute cycle, the FWT deduction for NRA employee's with Citizenship Status Code of "N" or "A" should be calculated by taking the employee's Federal Taxable Gross from the compute, adding a fixed amount to that value, and using the result to look up the tax in the Federal

Tax Table. The amount to be added to the gross is based on the employee's primary pay cycle:

\$ 102.00 – Biweekly
\$ 110.00 – Semi -Monthly
\$ 221.00 – Monthly

This amount must not be included in the employee's Federal taxable gross; it is used solely for purposes of calculating the FWT deduction amount.

This amount must not be included on Form W-2, Wage and Tax Statement or the Form 1042-S, Foreign Person's U.S. Source Income Subject to Withholding as it does not represent an actual increase to the employee's wages but as mentioned above is used solely for calculation of the FWT deduction.

IX. Online EDB Screens

The following online screens should be modified to remove the label "Addl Fed Nonres Alien Tax":

1. EALN

The EDB Entry/Update screen EALN "Alien Information" should be modified to remove the label "Addl Fed Nonres Alien Tax". With the removal of the label the field should be open for use. Attachment 1 contains a marked-up copy of the EALN screen.

2. ETAX

The EDB Entry/Update screen ETAX "Tax Information" should be modified to remove the label "Addl Fed Nonres Alien Tax". With the removal of the label the field should be open for use. Attachment 2 contains a marked-up copy of the ETAX screen.

3. ITAX

The EDB Inquiry screen ITAX "Tax Information" should be modified to remove the label "Addl Fed Nonres Alien Tax". With the removal of the label the field should be open for use. Attachment 3 contains a marked-up copy of the ITAX screen.

4. Web EDB Inquiry

The Web EDB Inquiry screen "Taxes" should be modified to remove the label "Nonres Alien Tax". With the removal of the label the field should be open for use. Attachment 4 contains a marked-up copy of the WEB tax screen.

X. Rush Checks/ORCA

These facilities should be modified to include the new procedures.

XI. Year-End Process

W-2 and 1042-S Processing

The new procedures have no effect on the W-2 or the 1042-S reporting process.

XII. History

There are no changes to the History Data Base screen IHW4. It should continue to carry the label “Addl Fed Nonres Alien Tax”.

XIII. Forms

The paper and web based version of Form UCW-4NR/DE4 will be revised by Payroll Coordination and Tax Services to remove statements regarding the additional NRA federal tax.

XIV. Supplemental Wage Payments

These new procedures for determining the amount of income tax withholding does not apply to supplemental wage payments. The current rate of 25 percent should continue to be used to determine the Federal tax withholding amount.

XV. Federal Insurance Contributions Act (FICA)

These changes have no effect on the FICA tax liability for the employer or the employee.

XVI. IDOC

There are no changes to the Summary of UC Benefits Enrollment or the Summary of Retirement and Savings Program Information IDOC process.

XVII. IVR

The GTN number 301 should be removed from the IVR deduction extract file.

XVIII. Special Student Processes

The special student processes 1 and 3 should be modified as follows:

- The special student process should be modified to NOT establish GTN 301 when a students Citizenship Status code changes from “S” to “N” or “R” to

“N” when the input interface files that compares information are run. These files are generally run at the beginning of summer and the beginning of the academic school year.

- The special student process should also be modified to NOT establish GTN 301 when a nonresident alien student UC Student Status code changes from 6² or 7 to 1 and the Citizenship Status code changes to “N”

XIX. Implementation

The changes must be implemented after check dates in December 2006 but before any check dated January 1, 2007.

² 1 - Not Registered

6 - Undergraduate student at another UC campus

7 - Graduate student at another UC campus

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Attachment 1

PPEALNO-ERRRR	EDB Entry/Update	09/28/01 09:39:29	
11/17/00 10:44:51	Alien Information	Userid: PAYUSR1	
ID: 000050069 Name: AGES,TRUDY		SSN: 555-61-7654 Pri Pay: BW	
Citizenship:	Country of Residence:	U.S. Date of Entry:	
Visa Type :	Work Permit End Date:		
Tax Treaty Income Code :	Alt Tax Treaty Income Code:		
Article Number:	Retirement System Code:		
End Date :	FICA Eligibility Code:		
Income Limit :	Ret FICA Derive:		
Federal Tax Marital Status:	Allowances:		
Maximum Withholding:	Additional Fed Withholding:		
Remove ? Addl Fed Nonres Alien Tax :			
Calif. Tax Marital Status:	Allowances:	Itemized Deductions:	
Maximum Withholding:	Additional CA Withholding :		
Non-UC Health Exp :	Non-Resident Alien Tax Form Indicator:		
Other State Tax CA Res :	Other State Name :	Local Tax:	
Next Func: ID:	Name:	SSN:	
===>			
F: 1-Help	3-PrevMenu	4-Print	5-Update
F:	9-Jump		12-Exit

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Attachment 2

```
PPETAX0-E1407          EDB Entry/Update          03/08/06 11:03:17
02/14/06 10:03:19      Tax Information          Userid: PAYUSR1
ID: 000050021 Name: BLUES, BERTHA D      Emp Stat: A      Pri Pay: MO
Federal
  Marital Status      : M      W-4 Process Date : 02/09/05
  Personal Allowances : 008      DE4 Process Date : 02/09/05
  Maximum Withholding : 010      Remove ? Addl Fed Nonres Alien Tax :
California
  Marital Status      : M
  Personal Allowances : 003
  Itemized Deductions : 002
  Maximum Withholding : 010
Addl Fed Tax Withholding :      25.00      Other State Tax CA Res :
Addl CA Tax Withholding :      15.00      Current OS Gross Name :
Other State Gross Name 1:
Earned Inc Credit Status :      Other State Gross Name 2:
EIC YTD Payments      :      Other State Gross Name 3:
Earnings Limit      :      Other Local Tax Ind :
SSN: 555555021
Next Func:      ID:      Name:      SSN:

===>
F: 1-Help      3-PrevMenu  4-Print      5-Update
F:      9-Jump      12-Exit
```

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Attachment 3

```
PPITAX0-I1656                      EDB Inquiry                      03/08/06
11:07:08
02/14/06 10:03:19          W-4/DE4 Tax Withholding          Userid:  PAYUSR1
ID: 000050021 Name: BLUES, BERTHA D
Hm Dept: 804918 CHAN OFFICE      Emplmt Status: A Pri Pay: MO
Federal                          Tax Processor ID : PPS02/09/05PAYPCW
  Marital Status                : M          W-4 Process Date : 02/09/05
  Personal Allowances           : 008        DE4 Process Date : 02/09/05
  Maximum Withholding           : 010      Remove ? Addl Fed Nonrs Alien Tax :
California
  Marital Status                : M
  Personal Allowances           : 003
  Itemized Deductions           : 002
  Maximum Withholding           : 010
Addl Fed Tax Withholding :      25.00 Current OS Gross Name :
Addl CA Tax Withholding  :      15.00 Other State Gross Name 1:
Earned Income Credit Stat:          Other State Gross Name 2:
EIC YTD Payments          :          Other State Gross Name 3:
Earnings Limit           :          Other Local Tax Ind:
SSN: 555555021
Next Func:      ID:          Name:          SSN:

===>
F:  1-Help      2-Browse      3-PrevMenu  4-Print
F:              9-MainMenu          12-Exit
```

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Attachment 4

Payroll/Personnel System - EDB Inquiry

Userid: PAYUSR1

Date: 07/10/06

Time: 10:38:52

Name: AGES,TRUDY

ID: 000050069

SSN: 555-61-7654

Status: Active

Home Dept: POMOLOGY

Pay Sched: Biweekly

Tax Information

Federal

Marital Status: S - Single

Allowances: 4

Maximum Allowances: 999

Additional Tax: 0.00

Remove? Non-Resident Alien
Tax:

YTD Taxable Gross: 6,731.14

YTD Taxes Withheld: 270.46

W-4 Process Date: 01/03/02

Tax Processor ID: PPS01/03/02PAYKLLK

OASDI

YTD Gross: 0.00

YTD Taxes Withheld: 0.00

Tax Treaty

YTD Tax Treaty Gross: 0.00

Alternate YTD Tax Treaty
Gross: 0.00

State

Marital Status: M - Married

Exemptions: 1

Itemized Deductions: 3

Maximum Allowances: 999

Additional Tax: 0.00

YTD Taxable Gross: 6,731.14

YTD Taxes Withheld: 43.44

DE4 Process Date:

Medicare

YTD Gross: 7,276.90

YTD Taxes Withheld: 105.52