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BACKUP WITHHOLDING
WHAT IS IT, AND HOW CAN I
OBTAIN A REFUND?

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INTRODUCTION

Many individuals who are neither citizens nor residents of the United States are surprised to find that they are nevertheless subject to U.S. tax rules and regulations on certain transactions. One of the more common instances where this happens is with respect to the so called “Backup Withholding Rule.” This memorandum will (i) provide some background relating to the backup withholding rule, and (ii) describe the steps for seeking a refund of any such withholding. The memorandum also provides in its appendices, references to forms necessary for seeking a refund of backup withholding and full text U.S. tax code sections that are applicable to the backup withholding rule.

I. BACKGROUND ON THE BACKUP WITHHOLDING RULE

The backup withholding rule is triggered where the U.S. Internal Revenue Service (“IRS”) suspects that some income may be subject to U.S. taxation and does not have the applicable documentary evidence to support an exemption. The reason for the rule is simple. In the absence of evidence to the contrary, the IRS will assume that income from U.S. activities are subject to tax and will do its best to capture those taxes.² There are several types of payments which the IRS has identified as being subject to backup withholding. These are interest, dividends, rents, royalties, commissions, non-employee compensation, and other payments including broker proceeds and barter exchange transactions, reportable gross proceeds paid to attorneys, and, for some reason, certain payments made by fishing boat operators.

There are also certain payments which are excluded from backup withholding. These include real estate transactions, foreclosures and abandonments, cancelled debts, distributions from Archer Medical Savings Accounts (MSAs), long-term care benefits, distributions from any retirement account, distributions from an employee stock ownership plan (ESOP), fish purchases for cash, unemployment compensation, state or local income tax refunds, and qualified tuition program earnings.

² 26 USC Sec. 31.

II. OBTAINING A REFUND OF BACKUP WITHHOLDING

In many cases, the IRS will issue a refund of backup withholding where no tax liability exists and where the proper filing and reporting obligations have been met. Ultimately, whether or not a refund can be obtained depends on the specific circumstances of each individual taxpayer. The following discussion gives a general overview of the steps that could result in the refund of backup withholding.

The backup withholding rule is typically triggered because the IRS believes it has insufficient documentation evidencing an exemption. This commonly occurs in three major instances: (i) the IRS does not have a proper taxpayer identification number (TIN) for the person receiving a payment (“payee”), (ii) Interest and dividend have been underreported, and (iii) “payee” has failed to comply with the proper certification procedures.³ The process of obtaining a refund for backup withholding will depend on the underlying reasons for the backup withholding rule being triggered.

(i) Refund for Backup Withholding due to Missing or Incorrect TIN

The most common scenario when backup withholding is triggered for non-U.S. persons is where the taxpayer has not furnished the IRS with a proper Taxpayer Identification Number (“TIN”). A TIN is the identification number used by the IRS in the administration of tax laws. Every filing made with the IRS must contain a TIN. For U.S. citizens and residents, the TIN will typically be a Social Security Number (SSN). For businesses registered or doing business in the U.S., the TIN will be an Employer Identification Number (EIN). Non-U.S. persons that have income derived from U.S. activities but are not eligible for an SSN or an EIN must apply to the IRS for an Individual Taxpayer Identification Number (ITIN). Where a TIN has not been submitted or where the submitted TIN does not match up with IRS records, the IRS will automatically assume that any connected U.S. income is subject to U.S. tax and will apply the backup withholding rule.⁴

A refund of backup withholding which was triggered by missing TIN can be obtained by the taxpayer filing the proper identification and information documentation with the IRS. This requires several steps:

³ 26 USC Sec. 3406(a)(1).

⁴ CFR. 31.3406(d)-5.

- First the payee must file for and obtain the proper ITIN using form W-7. Note that the payee will also have to notify the person providing payments to the payee (“payer”) once the payee receives an ITIN.
- Payee must complete form W-8BEN which certifies foreign status of the payee for the purposes of U.S. backup withholding. Note that the W-8BEN is not filed with the IRS but is provided to the payer. Note also that the W-8BEN requires a TIN.
- Payee must complete the necessary tax returns. In most cases for non-US persons, this will be Form 1040NR or Form 1040NR-EZ. Tax returns must generally be filed by April 15, or June 15 if place of business is not in the U.S.⁵

Upon completion of these steps and depending on the specifics of each case, the IRS may issue a refund of the backup withholding.

(ii) Refund for Backup Withholding due to Under Reporting of Interest and Dividend

Underreporting occurs when a payee fails to include in his tax return any portion of a reportable interest or dividend payment required to be shown or is required to file a return for that year, including a reportable interest or dividend payment in the return.⁶ Backup withholding then applies to any reportable interest or dividend payment made regarding a payee's account. Where such is the case, the IRS will typically notify the payer that the payee is subject to withholding due to under reporting⁷ and the payer in turn will notify the payee by sending a Backup Withholding Notice.⁸

To obtain a refund of backup withholding in the case of an under-reporting, a payee should file an amended income tax return, reporting all the income and the backup taxes that were withheld. Usually, a payer will provide payee with Form 1099 showing applicable income and any backup withholding taxes, reported as "Federal Income Tax Withheld". The payee should then file a tax return using form 1040NR or 1040NR-EZ as the case may be. The return should report, among other things, all investment income and the backup taxes withheld. Note

⁵ It is highly recommended that payees seek the aid of a qualified U.S. tax professional when preparing non resident tax returns.

⁶ CFR. 31.3406(c)-1(b)(2)

⁷ CFR. 31.3406(c)-1.

⁸ 26 USC Sec. 3406(b)(2).

that if the payee fails to file the return before the deadline for filing, a late filing penalty may be assessed. Once a return or amended return is filed, or if there was in fact no under reporting, a payee may prevent or stop future withholding by submitting a request for determination⁹ from the Internal Revenue Service based on at least one of the following grounds:

- no underreporting occurred;
- there is a bona fide dispute with the Internal Revenue Service about whether underreporting occurred;
- backup withholding will cause or is causing an undue hardship, and it is unlikely that interests and dividends will be underreported in the future and;
- an underreporting has been corrected by filing a return and all taxes, penalties and interests due has been paid¹⁰.

(iii) Refund for Backup Withholding due to Payee Certification Failure

Generally speaking, to prevent backup withholding a non-US person payee must furnish the payer with an accurate Form W-9, or acceptable substitute.¹¹ The form W-9 acts as a certification under penalty of perjury by payee that payee is not subject to backup withholding.¹² Where form W-9 has not been provided, the backup withholding rule is triggered and the payer will send a backup withholding notice (or “B-Notice”) to the payee.¹³ Once this notification has been received, the payee can prevent or stop the backup withholding by providing on Form W-9 or acceptable substitute, name and TIN and certification that taxpayer identification number is correct.¹⁴ A payer must stop withholding within 30 days of receiving a proper W-9 with TIN.¹⁵

Where a payer does not has not previously filed for and received a TIN from the IRS, the payee will not be able to provide the payer with a properly executed W-9. Where this is the case, the payer may attempt to obtain a refund of backup withholding by filing the proper informational and tax returns to the IRS as described in section II(i) supra.

⁹ CFR. 31.3406(c)-1(g)(1).

¹⁰ CFR. 31.3406(c)-1(g)(3).

¹¹ CFR. 31.3406(h)-3(e)(2).

¹² CFR. 31.3406(d)-2.

¹³ CFR. 31.3406(d)-3(c).

¹⁴ CFR. 31.3406(d)-5(f).

¹⁵ CFR. 31.3406(e)-2).

CONCLUSION

The foregoing was a general discussion designed to provide you with information about the possibility of receiving a refund of backup withholding. As you know, U.S. tax law is complex and each outcome depends on the specific facts and circumstances surrounding each individual taxpayer. Whereas this memorandum provides you with important background and information, it should not be taken as guaranteeing any specific outcome. It is highly recommended that you work with a qualified tax professional when dealing with the IRS.

APPENDIX 1: REFERENCED IRS FORMS¹⁶

Forms	Title
Form W-7	Application for IRS Individual Taxpayer Identification Number
Form W-8BEN	Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding
Form W-9	Request for Taxpayer Identification Number and Certification
Form 1040-NR	U.S. Nonresident Alien Income Tax Return
Form 1040-NR-EZ	U.S. Income Tax Return for Certain Nonresident Aliens With No Dependents
Form 1099	Miscellaneous Income

¹⁶ Most updated versions of IRS forms are available on the IRS website at: www.irs.gov

APPENDIX2: GOVERNING LAWS AND REGULATIONS

Sec. 3406. Backup withholding

TITLE 26, Subtitle C, CHAPTER 24, Sec. 3406.

- (a) Requirement to deduct and withhold
 - (1) In general
In the case of any reportable payment, if -
 - (A) the payee fails to furnish his TIN to the payor in the manner required,
 - (B) the Secretary notifies the payor that the TIN furnished by the payee is incorrect,
 - (C) there has been a notified payee underreporting described in subsection (c), or
 - (D) there has been a payee certification failure described in subsection (d), then the payor shall deduct and withhold from such payment a tax equal to the product of the fourth lowest rate of tax applicable under section 1(c) and such payment.
 - (2) Subparagraphs (C) and (D) of paragraph (1) apply only to interest and dividend payments
Subparagraphs (C) and (D) of paragraph (1) shall apply only to reportable interest or dividend payments.
- (b) Reportable payment, etc.
For purposes of this section -
 - (1) Reportable payment
The term "reportable payment" means -
 - (A) any reportable interest or dividend payment, and
 - (B) any other reportable payment.
 - (2) Reportable interest or dividend payment
 - (A) In general
The term "reportable interest or dividend payment" means any payment of a kind, and to a payee, required to be shown on a return required under -
 - (i) section 6049(a) (relating to payments of interest),
 - (ii) section 6042(a) (relating to payments of dividends), or
 - (iii) section 6044 (relating to payments of patronage dividends) but only to the extent such payment is in money.
 - (B) Special rule for patronage dividends
For purposes of subparagraphs (C) and (D) of subsection (a)(1), the term "reportable interest or dividend payment" shall not include any payment to which section 6044 (relating to patronage dividends) applies unless 50 percent or more of such payment is in money.
 - (3) Other reportable payment
The term "other reportable payment" means any payment of a kind, and to a payee, required to be shown on a return required under -

- (A) section 6041 (relating to certain information at source),
 - (B) section 6041A(a) (relating to payments of remuneration for services),
 - (C) section 6045 (relating to returns of brokers),
 - (D) section 6050A (relating to reporting requirements of certain fishing boat operators), but only to the extent such payment is in money and represents a share of the proceeds of the catch, or
 - (E) section 6050N (relating to payments of royalties).
- (4) Whether payment is of reportable kind determined without regard to minimum amount
The determination of whether any payment is of a kind required to be shown on a return described in paragraph (2) or (3) shall be made without regard to any minimum amount which must be paid before a return is required.
- (5) Exception for certain small payments
To the extent provided in regulations, the term "reportable payment" shall not include any payment which -
- (A) does not exceed \$10, and
 - (B) if determined for a 1-year period, would not exceed \$10.
- (6) Other reportable payments include payments described in section 6041(a) or 6041A(a) only where aggregate for calendar year is \$600 or more
Any payment of a kind required to be shown on a return required under section 6041(a) or 6041A(a) which is made during any calendar year shall be treated as a reportable payment only if -
- (A) the aggregate amount of such payment and all previous payments described in such sections by the payor to the payee during such calendar year equals or exceeds \$600,
 - (B) the payor was required under section 6041(a) or 6041A(a) to file a return for the preceding calendar year with respect to payments to the payee, or
 - (C) during the preceding calendar year, the payor made reportable payments to the payee with respect to which amounts were required to be deducted and withheld under subsection (a).
- (7) Exception for certain window payments of interest, etc.
For purposes of subparagraphs (C) and (D) of subsection (a)(1), the term "reportable interest or dividend payment" shall not include any payment -
- (A) in redemption of a coupon on a bearer instrument or in redemption of a United States savings bond, or
 - (B) to the extent provided in regulations, of interest on instruments similar to those described in subparagraph (A). The preceding sentence shall not apply for purposes of determining whether there is payee underreporting described in subsection (c).
- (c) Notified payee underreporting with respect to interest and dividends

- (1) Notified payee underreporting**
If -
- (A)** the Secretary determines with respect to any payee that there has been payee underreporting,
 - (B)** at least 4 notices have been mailed by the Secretary to the payee (over a period of at least 120 days) with respect to the underreporting, and
 - (C)** in the case of any payee who has filed a return for the taxable year, any deficiency of tax attributable to such failure has been assessed, the Secretary may notify payors of reportable interest or dividend payments with respect to such payee of the requirement to deduct and withhold under subsection (a)(1)(C) (but not the reasons for the withholding under subsection (a)(1)(C)).
- (2) Payee underreporting defined**
For purposes of this section, there has been payee underreporting if for any taxable year the Secretary determines that -
- (A)** the payee failed to include in his return of tax under chapter 1 for such year any portion of a reportable interest or dividend payment required to be shown on such return, or
 - (B)** the payee may be required to file a return for such year and to include a reportable interest or dividend payment in such return, but failed to file such return.
- (3) Determination by secretary to stop (or not to start) withholding**
- (A) In general**
If the Secretary determines that -
 - (i)** there was no payee underreporting,
 - (ii)** any payee underreporting has been corrected (and any tax, penalty, or interest with respect to the payee underreporting has been paid),
 - (iii)** withholding under subsection (a)(1)(C) has caused (or would cause) undue hardship to the payee and it is unlikely that any payee underreporting by such payee will occur again, or
 - (iv)** there is a bona fide dispute as to whether there has been any payee underreporting, then the Secretary shall take the action described in subparagraph (B).
 - (B) Secretary to take action to stop (or not to start) withholding**
For purposes of subparagraph (A), if at the time of the Secretary's determination under subparagraph (A) -
 - (i)** no notice has been given under paragraph (1) to any payor with respect to the underreporting, the Secretary shall not give any such notice, or
 - (ii)** if such notice has been given, the Secretary shall -
 - (I)** provide the payee with a written certification that withholding under subsection (a)(1)(C) is to stop, and

- (II)** notify the applicable payors (and brokers) that such withholding is to stop.
- (C)** Time for taking action where notice to payor has been given

In any case where notice has been given under paragraph (1) to any payor with respect to any underreporting, if the Secretary makes a determination under subparagraph (A) during the 12-month period ending on October 15 of any calendar year -

 - (i)** except as provided in clause (ii), the Secretary shall take the action described in subparagraph (B)(ii) to bring about the stopping of withholding no later than December 1 of such calendar year, or
 - (ii)** in the case of -
 - (I)** a no payee underreporting determination under clause (i) of subparagraph (A), or
 - (II)** a hardship determination under clause (iii) of subparagraph (A), such action shall be taken no later than the 45th day after the day on which the Secretary made the determination.
- (D)** Opportunity to request determination

The Secretary shall prescribe procedures under which -

 - (i)** a payee may request a determination under subparagraph (A), and
 - (ii)** the payee may provide information with respect to such request.
- (4)** Payor notifies payee of withholding because of payee underreporting

Any payor required to withhold any tax under subsection (a)(1)(C) shall, at the time such withholding begins, notify the payee of such withholding.
- (5)** Payee may be required to notify Secretary who his payors and brokers are

For purposes of this section, the Secretary may require any payee of reportable interest or dividend payments who is subject to withholding under subsection (a)(1)(C) to notify the Secretary of -

 - (A)** all payors from whom the payee receives reportable interest or dividend payments, and
 - (B)** all brokers with whom the payee has accounts which may involve reportable interest or dividend payments. The Secretary may notify any such broker that such payee is subject to withholding under subsection (a)(1)(C).
- (d)** Interest and dividend backup withholding applies to new accounts and instruments unless payee certifies that he is not subject to such withholding
 - (1)** In general

There is a payee certification failure unless the payee has certified to the payor, under penalty of perjury, that such payee is not subject to withholding under subsection (a)(1)(C).
 - (2)** Special rules for readily tradable instruments

- (A) In general**
 Subsection (a)(1)(D) shall apply to any reportable interest or dividend payment to any payee on any readily tradable instrument if (and only if) the payor was notified by a broker under subparagraph (B) or no certification was provided to the payor by the payee under paragraph (1) and -
- (i)** such instrument was acquired directly by the payee from the payor, or
 - (ii)** such instrument is held by the payor as nominee for the payee.
- (B) Broker notifies payor**
 If -
- (i)** a payee acquires any readily tradable instrument through a broker, and
 - (ii)** with respect to such acquisition -
- (I)** the payee fails to furnish his TIN to the broker in the manner required under subsection (a)(1)(A),
 - (II)** the Secretary notifies such broker before such acquisition that the TIN furnished by the payee is incorrect,
 - (III)** the Secretary notifies such broker before such acquisition that such payee is subject to withholding under subsection (a)(1)(C), or
 - (IV)** the payee does not provide a certification to such broker under subparagraph (C), such broker shall, within such period as the Secretary may prescribe by regulations (but not later than 15 days after such acquisition), notify the payor that such payee is subject to withholding under subparagraph (A), (B), (C), or (D) of subsection (a)(1), respectively.
- (C) Time for payee to provide certification to broker**
 In the case of any readily tradable instrument acquired by a payee through a broker, the certification described in paragraph (1) may be provided by the payee to such broker -
- (i)** at any time after the payee's account with the broker was established and before the acquisition of such instrument, or
 - (ii)** in connection with the acquisition of such instrument.
- (3) Exception for existing accounts, etc.**
 This subsection and subsection (a)(1)(D) shall not apply to any reportable interest or dividend payment which is paid or credited -
- (A)** in the case of interest or any other amount of a kind reportable under section 6049, with respect to any account (whatever called) established before January 1, 1984, or with respect to any instrument acquired before January 1, 1984,
 - (B)** in the case of dividends or any other amount reportable under section 6042, on any stock or other instrument acquired before January 1, 1984, or
 - (C)** in the case of patronage dividends or other amounts of a kind reportable under section 6044, with respect to any membership acquired, or contract entered into, before January 1, 1984.

- (4) Exception for readily tradable instruments acquired through existing brokerage accounts**
 Subparagraph (B) of paragraph (2) shall not apply with respect to a readily tradable instrument which was acquired through an account with a broker if -
- (A)** such account was established before January 1, 1984, and
 - (B)** during 1983, such broker bought or sold instruments for the payee (or acted as a nominee for the payee) through such account. The preceding sentence shall not apply with respect to any readily tradable instrument acquired through such account after the broker was notified by the Secretary that the payee is subject to withholding under subsection (a)(1)(C).
- (e) Period for which withholding is in effect**
- (1) Failure to furnish TIN**
 In the case of any failure by a payee to furnish his TIN to a payor in the manner required, subsection (a) shall apply to any reportable payment made by such payor during the period during which the TIN has not been furnished in the manner required. The Secretary may require that a TIN required to be furnished under subsection (a)(1)(A) be provided under penalties of perjury only with respect to interest, dividends, patronage dividends, and amounts subject to broker reporting.
 - (2) Notification of incorrect number**
 In any case in which the Secretary notifies the payor that the TIN furnished by the payee is incorrect, subsection (a) shall apply to any reportable payment made by such payor -
 - (A)** after the close of the 30th day after the day on which the payor received such notification, and
 - (B)** before the payee furnishes another TIN in the manner required.
 - (3) Notified payee underreporting described in subsection (c)**
 - (A) In general**
 In the case of any notified payee underreporting described in subsection (c), subsection (a) shall apply to any reportable interest or dividend payment made -
 - (i)** after the close of the 30th day after the day on which the payor received notification from the Secretary of such underreporting, and
 - (ii)** before the stop date.
 - (B) Stop date**
 For purposes of this subsection, the term "stop date" means the determination effective date or, if later, the earlier of -
 - (i)** the day on which the payor received notification from the Secretary under subsection (c)(3)(B) to stop withholding, or
 - (ii)** the day on which the payor receives from the payee a certification provided by the Secretary under subsection (c)(3)(B).

- (C) Determination effective date**
For purposes of this subsection -
- (i) In general**
Except as provided in clause (ii), the determination effective date of any determination under subsection (c)(3)(A) which is made during the 12-month period ending on October 15 of any calendar year shall be the first January 1 following such October 15.
 - (ii) Determination that there was no underreporting; hardship**
In the case of any determination under clause (i) or (iii) of subsection (c)(3)(A), the determination effective date shall be the date on which the Secretary's determination is made.
- (4) Failure to provide certification that payee is not subject to withholding**
- (A) In general**
In the case of any payee certification failure described in subsection (d)(1), subsection (a) shall apply to any reportable interest or dividend payment made during the period during which the certification described in subsection (d)(1) has not been furnished to the payor.
 - (B) Special rule for readily tradable instruments acquired through broker where notification**
In the case of any readily tradable instrument acquired by the payee through a broker, the period described in subparagraph (A) shall start with payments to the payee made after the close of the 30th day after the payor receives notification from a broker under subsection (d)(2)(B).
- (5) 30-day grace periods**
- (A) Start-up**
If the payor elects the application of this subparagraph with respect to the payee, subsection (a) shall also apply to any reportable payment made during the 30-day period described in paragraph (2)(A), (3)(A), or (4)(B).
 - (B) Stopping**
Unless the payor elects not to have this subparagraph apply with respect to the payee, subsection (a) shall also apply to any reportable payment made after the close of the period described in paragraph (1), (2), or (4) (as the case may be) and before the 30th day after the close of such period. A similar rule shall also apply with respect to the period described in paragraph (3)(A) where the stop date is determined under clause (i) or (ii) of paragraph (3)(B).
- (C) Election of shorter grace period**
The payor may elect a period shorter than the grace period set forth in subparagraph (A) or (B), as the case may be.
- (f) Confidentiality of information**
- (1) In general**
No person may use any information obtained under this section (including any failure

to certify under subsection (d)) except for purposes of meeting any requirement under this section or (subject to the safeguards set forth in section 6103) for purposes permitted under section 6103.

- (2) Cross reference**
For provision providing for civil damages for violation of paragraph (1), see section 7431.
- (g) Exceptions**

 - (1) Payments to certain payees**
Subsection (a) shall not apply to any payment made to -

 - (A)** any organization or governmental unit described in subparagraph (B), (C), (D), (E), or (F) of section 6049(b)(4), or
 - (B)** any other person specified in regulations.
 - (2) Amounts for which withholding otherwise required**
Subsection (a) shall not apply to any amount for which withholding is otherwise required by this title.
 - (3) Exemption while waiting for TIN**
The Secretary shall prescribe regulations for exemptions from the tax imposed by subsection (a) during the period during which a person is waiting for receipt of a TIN.
 - (h) Other definitions and special rules**
For purposes of this section -

 - (1) Obviously incorrect number**
A person shall be treated as failing to furnish his TIN if the TIN furnished does not contain the proper number of digits.
 - (2) Payee furnishes 2 incorrect TINs**
If the payee furnishes the payor 2 incorrect TINs in any 3-year period, the payor shall, after receiving notice of the second incorrect TIN, treat the payee as not having furnished another TIN under subsection (e)(2)(B) until the day on which the payor receives notification from the Secretary that a correct TIN has been furnished.
 - (3) Joint payees**
Except to the extent otherwise provided in regulations, any payment to joint payees shall be treated as if all the payment were made to the first person listed in the payment.
 - (4) Payor defined**
The term "payor" means, with respect to any reportable payment, a person required to file a return described in paragraph (2) or (3) of subsection (b) with respect to such payment.
 - (5) Broker**

 - (A) In general**
The term "broker" has the meaning given to such term by section 6045(c)(1).

- (B) Only 1 broker per acquisition
If, but for this subparagraph, there would be more than 1 broker with respect to any acquisition, only the broker having the closest contact with the payee shall be treated as the broker.
- (C) Payor not treated as broker
In the case of any instrument, such term shall not include any person who is the payor with respect to such instrument.
- (D) Real estate broker not treated as a broker
Except as provided by regulations, such term shall not include any real estate broker (as defined in section 6045(e)(2)).
- (6) Readily tradable instrument
The term "readily tradable instrument" means -
 - (A) any instrument which is part of an issue any portion of which is traded on an established securities market (within the meaning of section 453(f)(5)), and
 - (B) except as otherwise provided in regulations prescribed by the Secretary, any instrument which is regularly quoted by brokers or dealers making a market.
- (7) Original issue discount
To the extent provided in regulations, rules similar to the rules of paragraph (6) of section 6049(d) shall apply.
- (8) Requirement of notice to payee
Whenever the Secretary notifies a payor under paragraph (1)(B) of subsection (a) that the TIN furnished by any payee is incorrect, the Secretary shall at the same time furnish a copy of such notice to the payor, and the payor shall promptly furnish such copy to the payee.
- (9) Requirement of notice to Secretary
If the Secretary notifies a payor under paragraph (1)(B) of subsection (a) that the TIN furnished by any payee is incorrect and such payee subsequently furnishes another TIN to the payor, the payor shall promptly notify the Secretary of the other TIN so furnished.
- (10) Coordination with other sections
For purposes of section 31, this chapter (other than section 3402(n)), and so much of subtitle F (other than section 7205) as relates to this chapter, payments which are subject to withholding under this section shall be treated as if they were wages paid by an employer to an employee (and amounts deducted and withheld under this section shall be treated as if deducted and withheld under section 3402).
- (i) Regulations
The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.

Sec. 1441. Withholding of tax on nonresident aliens

TITLE 26, Subtitle A, CHAPTER 3, Subchapter A, Sec. 1441.

(a) General rule

Except as otherwise provided in subsection (c), all persons, in whatever capacity acting (including lessees or mortgagors of real or personal property, fiduciaries, employers, and all officers and employees of the United States) having the control, receipt, custody, disposal, or payment of any of the items of income specified in subsection (b) (to the extent that any of such items constitutes gross income from sources within the United States), of any nonresident alien individual or of any foreign partnership shall (except as otherwise provided in regulations prescribed by the Secretary under section 874) deduct and withhold from such items a tax equal to 30 percent thereof, except that in the case of any item of income specified in the second sentence of subsection (b), the tax shall be equal to 14 percent of such item.

(b) Income items

The items of income referred to in subsection (a) are interest (other than original issue discount as defined in section 1273), dividends, rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income, gains described in section 631(b) or (c), amounts subject to tax under section 871(a)(1)(C), gains subject to tax under section 871(a)(1)(D), and gains on transfers described in section 1235 made on or before October 4, 1966. The items of income referred to in subsection (a) from which tax shall be deducted and withheld at the rate of 14 percent are amounts which are received by a nonresident alien individual who is temporarily present in the United States as a nonimmigrant under subparagraph (F), (J), (M), or (Q) of section 101(a)(15) of the Immigration and Nationality Act and which are -

(1) incident to a qualified scholarship to which section 117(a) applies, but only to the extent includible in gross income; or

(2) in the case of an individual who is not a candidate for a degree at an educational organization described in section 170(b)(1)(A)(ii), granted by -

(A) an organization described in section 501(c)(3) which is exempt from tax under section 501(a),

(B) a foreign government,

(C) an international organization, or a binational or multinational educational and cultural foundation or commission created or continued pursuant to the Mutual Educational and Cultural Exchange Act of 1961, or

(D) the United States, or an instrumentality or agency thereof, or a State, or a possession of the United States, or any political subdivision thereof, or the District of Columbia, as a scholarship or fellowship for study, training, or research in the United States. In the case of a nonresident alien individual who is a member of a domestic partnership, the items of income referred to in subsection (a) shall be treated as referring to items specified in this subsection included in his distributive share of the income of such partnership.

(c) Exceptions

(1) Income connected with United States business

No deduction or withholding under subsection (a) shall be required in the case of any

item of income (other than compensation for personal services) which is effectively connected with the conduct of a trade or business within the United States and which is included in the gross income of the recipient under section 871(b)(2) for the taxable year.

(2) Owner unknown

The Secretary may authorize the tax under subsection (a) to be deducted and withheld from the interest upon any securities the owners of which are not known to the withholding agent.

(3) Bonds with extended maturity dates

The deduction and withholding in the case of interest on bonds, mortgages, or deeds of trust or other similar obligations of a corporation, within subsections (a), (b), and (c) of section 1451 (as in effect before its repeal by the Tax Reform Act of 1984) were it not for the fact that the maturity date of such obligations has been extended on or after January 1, 1934, and the liability assumed by the debtor exceeds 27 1/2 percent of the interest, shall not exceed the rate of 27 1/2 percent per annum.

(4) Compensation of certain aliens

Under regulations prescribed by the Secretary, compensation for personal services may be exempted from deduction and withholding under subsection (a).

(5) Special items

In the case of gains described in section 631(b) or (c), gains subject to tax under section 871(a)(1)(D), and gains on transfers described in section 1235 made on or before October 4, 1966, the amount required to be deducted and withheld shall, if the amount of such gain is not known to the withholding agent, be such amount, not exceeding 30 percent of the amount payable, as may be necessary to assure that the tax deducted and withheld shall not be less than 30 percent of such gain.

(6) Per diem of certain aliens

No deduction or withholding under subsection (a) shall be required in the case of amounts of per diem for subsistence paid by the United States Government (directly or by contract) to any nonresident alien individual who is engaged in any program of training in the United States under the Mutual Security Act of 1954, as amended.

(7) Certain annuities received under qualified plans

No deduction or withholding under subsection (a) shall be required in the case of any amount received as an annuity if such amount is, under section 871(f), exempt from the tax imposed by section 871(a).

(8) Original issue discount

The Secretary may prescribe such regulations as may be necessary for the deduction and withholding of the tax on original issue discount subject to tax under section 871(a)(1)(C) including rules for the deduction and withholding of the tax on original issue discount from payments of interest.

(9) Interest income from certain portfolio debt investments

In the case of portfolio interest (within the meaning of section 871(h)), no tax shall be required to be deducted and withheld from such interest unless the person required to

deduct and withhold tax from such interest knows, or has reason to know, that such interest is not portfolio interest by reason of section 871(h)(3) or (4).

(10) Exception for certain interest and dividends

No tax shall be required to be deducted and withheld under subsection (a) from any amount described in section 871(i)(2).

(11) Certain gambling winnings

No tax shall be required to be deducted and withheld under subsection (a) from any amount exempt from the tax imposed by section 871(a)(1)(A) by reason of section 871(j).

(d) Exemption of certain foreign partnerships

Subject to such terms and conditions as may be provided by regulations prescribed by the Secretary, subsection (a) shall not apply in the case of a foreign partnership engaged in trade or business within the United States if the Secretary determines that the requirements of subsection (a) impose an undue administrative burden and that the collection of the tax imposed by section 871(a) on the members of such partnership who are nonresident alien individuals will not be jeopardized by the exemption.

(e) Alien resident of Puerto Rico

For purposes of this section, the term "nonresident alien individual" includes an alien resident of Puerto Rico.

(f) Continental shelf areas

For sources of income derived from, or for services performed with respect to, the exploration or exploitation of natural resources on submarine areas adjacent to the territorial waters of the United States, see section 638.

(g) Cross reference

For provision treating 85 percent of social security benefits as subject to withholding under this section, see section 871(a)(3).

Sec. 1442. Withholding of tax on foreign corporations

TITLE 26, Subtitle A, CHAPTER 3, Subchapter A, Sec. 1442.

(a) General rule

In the case of foreign corporations subject to taxation under this subtitle, there shall be deducted and withheld at the source in the same manner and on the same items of income as is provided in section 1441 a tax equal to 30 percent thereof. For purposes of the preceding sentence, the references in section 1441(b) to sections 871(a)(1)(C) and (D) shall be treated as referring to sections 881(a)(3) and (4), the reference in section 1441(c)(1) to section 871(b)(2) shall be treated as referring to section 842 or section 882(a)(2), as the case may be, the reference in section 1441(c)(5) to section 871(a)(1)(D) shall be treated as referring to section 881(a)(4), the reference in section 1441(c)(8) to section 871(a)(1)(C) shall be treated as referring to section 881(a)(3), the references in section 1441(c)(9) to sections 871(h) and 871(h)(3) or (4) shall be treated

as referring to sections 881(c) and 881(c)(3) or (4), and the reference in section 1441(c)(10) to section 871(i)(2) shall be treated as referring to section 881(d).

(b) Exemption

Subject to such terms and conditions as may be provided by regulations prescribed by the Secretary, subsection (a) shall not apply in the case of a foreign corporation engaged in trade or business within the United States if the Secretary determines that the requirements of subsection (a) impose an undue administrative burden and that the collection of the tax imposed by section 881 on such corporation will not be jeopardized by the exemption.

(c) Exception for certain possessions corporations

For purposes of this section, the term "foreign corporation" does not include a corporation created or organized in Guam, American Samoa, the Northern Mariana Islands, or the Virgin Islands or under the law of any such possession if the requirements of subparagraphs (A), (B), and (C) of section 881(b)(1) are met with respect to such corporation.

Sec. 1446. Withholding¹ tax on foreign partners' share of effectively connected income

TITLE 26, Subtitle A, CHAPTER 3, Subchapter A, Sec. 1446.

(a) General rule

If -

- (1)** a partnership has effectively connected taxable income for any taxable year, and
- (2)** any portion of such income is allocable under section 704 to a foreign partner, such partnership shall pay a withholding tax under this section at such time and in such manner as the Secretary shall by regulations prescribe.

(b) Amount of withholding tax

(1) In general

The amount of the withholding tax payable by any partnership under subsection (a) shall be equal to the applicable percentage of the effectively connected taxable income of the partnership which is allocable under section 704 to foreign partners.

(2) Applicable percentage

For purposes of paragraph (1), the term "applicable percentage" means -

- (A)** the highest rate of tax specified in section 1 in the case of the portion of the effectively connected taxable income which is allocable under section 704 to foreign partners who are not corporations, and
- (B)** the highest rate of tax specified in section 11(b)(1) in the case of the portion of the effectively connected taxable income which is allocable under section 704 to foreign partners which are corporations.

(c) Effectively connected taxable income

For purposes of this section, the term "effectively connected taxable income" means the taxable income of the partnership which is effectively connected (or treated as

effectively connected) with the conduct of a trade or business in the United States computed with the following adjustments:

- (1) Paragraph (1) of section 703(a) shall not apply.
- (2) The partnership shall be allowed a deduction for depletion with respect to oil and gas wells but the amount of such deduction shall be determined without regard to sections 613 and 613A.
- (3) There shall not be taken into account any item of income, gain, loss, or deduction to the extent allocable under section 704 to any partner who is not a foreign partner.
- (d) Treatment of foreign partners
 - (1) Allowance of credit

Each foreign partner of a partnership shall be allowed a credit under section 33 for such partner's share of the withholding tax paid by the partnership under this section. Such credit shall be allowed for the partner's taxable year in which (or with which) the partnership taxable year (for which such tax was paid) ends.
 - (2) Credit treated as distributed to partner

Except as provided in regulations, a foreign partner's share of any withholding tax paid by the partnership under this section shall be treated as distributed to such partner by such partnership on the earlier of -

 - (A) the day on which such tax was paid by the partnership, or
 - (B) the last day of the partnership's taxable year for which such tax was paid.
- (e) Foreign partner

For purposes of this section, the term "foreign partner" means any partner who is not a United States person.
- (f) Regulations

The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this section, including -

 - (1) regulations providing for the application of this section in the case of publicly traded partnerships, and
 - (2) regulations providing -
 - (A) that, for purposes of section 6655, the withholding tax imposed under this section shall be treated as a tax imposed by section 11 and any partnership required to pay such tax shall be treated as a corporation, and
 - (B) appropriate adjustments in applying section 6655 with respect to such withholding tax.

Sec. 1462. Withheld tax as credit to recipient of income

TITLE 26, Subtitle A, CHAPTER 3, Subchapter B, Sec. 1462.

Income on which any tax is required to be withheld at the source under this chapter shall be

included in the return of the recipient of such income, but any amount of tax so withheld shall be credited against the amount of income tax as computed in such return.

Sec. 1464. Refunds and credits with respect to withheld tax

TITLE 26, Subtitle A, CHAPTER 3, Subchapter B, Sec. 1464.

Where there has been an overpayment of tax under this chapter, any refund or credit made under chapter 65 shall be made to the withholding agent unless the amount of such tax was actually withheld by the withholding agent.

Sec. 31. Tax withheld on wages

TITLE 26, Subtitle A, CHAPTER 1, Subchapter A, PART IV, Subpart C, Sec. 31.

(a) Wage withholding for income tax purposes

(1) In general

The amount withheld as tax under chapter 24 shall be allowed to the recipient of the income as a credit against the tax imposed by this subtitle.

(2) Year of credit

The amount so withheld during any calendar year shall be allowed as a credit for the taxable year beginning in such calendar year. If more than one taxable year begins in a calendar year, such amount shall be allowed as a credit for the last taxable year so beginning.

(b) Credit for special refunds of social security tax

(1) In general

The Secretary may prescribe regulations providing for the crediting against the tax imposed by this subtitle of the amount determined by the taxpayer or the Secretary to be allowable under section 6413(c) as a special refund of tax imposed on wages. The amount allowed as a credit under such regulations shall, for purposes of this subtitle, be considered an amount withheld at source as tax under section 3402.

(2) Year of credit

Any amount to which paragraph (1) applies shall be allowed as a credit for the taxable year beginning in the calendar year during which the wages were received. If more than one taxable year begins in the calendar year, such amount shall be allowed as a credit for the last taxable year so beginning.

(c) Special rule for backup withholding

Any credit allowed by subsection (a) for any amount withheld under section 3406 shall be allowed for the taxable year of the recipient of the income in which the income is received.

Sec. 33. Tax withheld at source on nonresident aliens and foreign corporations

TITLE 26, Subtitle A, CHAPTER 1, Subchapter A, PART IV, Subpart C, Sec. 33.

There shall be allowed as a credit against the tax imposed by this subtitle the amount of tax withheld at source under subchapter A of chapter 3 (relating to withholding of tax on nonresident aliens and on foreign corporations).

Sec. 874. Allowance of deductions and credits

TITLE 26, Subtitle A, CHAPTER 1, Subchapter N, PART II, Subpart A, Sec. 874.

(a) Return prerequisite to allowance

A nonresident alien individual shall receive the benefit of the deductions and credits allowed to him in this subtitle only by filing or causing to be filed with the Secretary a true and accurate return, in the manner prescribed in subtitle F (sec. 6001 and following, relating to procedure and administration), including therein all the information which the Secretary may deem necessary for the calculation of such deductions and credits. This subsection shall not be construed to deny the credits provided by sections 31 and 33 for tax withheld at source or the credit provided by section 34 for certain uses of gasoline and special fuels.

(b) Tax withheld at source

The benefit of the deduction for exemptions under section 151 may, in the discretion of the Secretary, and under regulations prescribed by the Secretary, be received by a nonresident alien individual entitled thereto, by filing a claim therefor with the withholding agent.

(c) Foreign tax credit

Except as provided in section 906, a nonresident alien individual shall not be allowed the credits against the tax for taxes of foreign countries and possessions of the United States allowed by section 901.

Sec. 882. Tax on income of foreign corporations connected with United States business

TITLE 26, Subtitle A, CHAPTER 1, Subchapter N, PART II, Subpart B, Sec. 882.

(a) Imposition of tax

(1) In general

A foreign corporation engaged in trade or business within the United States during the taxable year shall be taxable as provided in section 11, 55, 59A, or 1201(a) on its taxable income which is effectively connected with the conduct of a trade or business within the United States.

(2) Determination of taxable income

In determining taxable income for purposes of paragraph (1), gross income includes only gross income which is effectively connected with the conduct of a trade or business within the United States.

(3) [Cross reference¹]

For special tax treatment of gain or loss from the disposition by a foreign corporation of a United States real property interest, see section 897.

(b) Gross income

In the case of a foreign corporation, except where the context clearly indicates otherwise, gross income includes only -

- (1)** gross income which is derived from sources within the United States and which is not effectively connected with the conduct of a trade or business within the United States, and
- (2)** gross income which is effectively connected with the conduct of a trade or business within the United States.

(c) Allowance of deductions and credits

(1) Allocation of deductions

(A) General rule

In the case of a foreign corporation, the deductions shall be allowed only for purposes of subsection (a) and (except as provided by subparagraph (B)) only if and to the extent that they are connected with income which is effectively connected with the conduct of a trade or business within the United States; and the proper apportionment and allocation of the deductions for this purpose shall be determined as provided in regulations prescribed by the Secretary.

(B) Charitable contributions

The deduction for charitable contributions and gifts provided by section 170 shall be allowed whether or not connected with income which is effectively connected with the conduct of a trade or business within the United States.

(2) Deductions and credits allowed only if return filed

A foreign corporation shall receive the benefit of the deductions and credits allowed to it in this subtitle only by filing or causing to be filed with the Secretary a true and accurate return, in the manner prescribed in subtitle F, including therein all the information which the Secretary may deem necessary for the calculation of such deductions and credits. The preceding sentence shall not apply for purposes of the tax imposed by section 541 (relating to personal holding company tax), and shall not be construed to deny the credit provided by section 33 for tax withheld at source or the credit provided by section 34 for certain uses of gasoline.

(3) Foreign tax credit

Except as provided by section 906, foreign corporations shall not be allowed the credit against the tax for taxes of foreign countries and possessions of the United States allowed by section 901.

(4) Cross reference

For rule that certain foreign taxes are not to be taken into account in determining deduction or credit, see section 906(b)(1).

(d) Election to treat real property income as income connected with United States business

(1) In general

A foreign corporation which during the taxable year derives any income -

- (A) from real property located in the United States, or from any interest in such real property, including (i) gains from the sale or exchange of real property or an interest therein, (ii) rents or royalties from mines, wells, or other natural deposits, and (iii) gains described in section 631(b) or (c), and
- (B) which, but for this subsection, would not be treated as income effectively connected with the conduct of a trade or business within the United States, may elect for such taxable year to treat all such income as income which is effectively connected with the conduct of a trade or business within the United States. In such case, such income shall be taxable as provided in subsection (a)(1) whether or not such corporation is engaged in trade or business within the United States during the taxable year. An election under this paragraph for any taxable year shall remain in effect for all subsequent taxable years, except that it may be revoked with the consent of the Secretary with respect to any taxable year.
- (2) Election after revocation, etc.
Paragraphs (2) and (3) of section 871(d) shall apply in respect of elections under this subsection in the same manner and to the same extent as they apply in respect of elections under section 871(d).
- (e) Interest on United States obligations received by banks organized in possessions
In the case of a corporation created or organized in, or under the law of, a possession of the United States which is carrying on the banking business in a possession of the United States, interest on obligations of the United States which is not portfolio interest (as defined in section 881(c)(2)) shall -
 - (1) for purposes of this subpart, be treated as income which is effectively connected with the conduct of a trade or business within the United States, and
 - (2) shall be taxable as provided in subsection (a)(1) whether or not such corporation is engaged in trade or business within the United States during the taxable year.
- (f) Returns of tax by agent
If any foreign corporation has no office or place of business in the United States but has an agent in the United States, the return required under section 6012 shall be made by the agent.

Sec. 6401. Amounts treated as overpayments

TITLE 26, Subtitle F, CHAPTER 65, Subchapter A, Sec. 6401.

- (a) Assessment and collection after limitation period.
The term "overpayment" includes that part of the amount of the payment of any internal revenue tax which is assessed or collected after the expiration of the period of limitation properly applicable thereto.
- (b) Excessive credits
 - (1) In general
If the amount allowable as credits under subpart C of part IV of subchapter A of

chapter 1 (relating to refundable credits) exceeds the tax imposed by subtitle A (reduced by the credits allowable under subparts A, B, D, and G of such part IV), the amount of such excess shall be considered an overpayment.

(2) Special rule for credit under section 33

For purposes of paragraph (1), any credit allowed under section 33 (relating to withholding of tax on nonresident aliens and on foreign corporations) for any taxable year shall be treated as a credit allowable under subpart C of part IV of subchapter A of chapter 1 only if an election under subsection (g) or (h) of section 6013 is in effect for such taxable year. The preceding sentence shall not apply to any credit so allowed by reason of section 1446.

(c) Rule where no tax liability

An amount paid as tax shall not be considered not to constitute an overpayment solely by reason of the fact that there was no tax liability in respect of which such amount was paid.

CFR. 31.3406(h)-3(e)(2)

(e) *Reasonable reliance on certificate* —(1) *In general.* A payor is not liable for the tax imposed under section 3406 if the payor's failure to deduct and withhold the tax is due to reasonable reliance, as defined in paragraph (e)(2) of this section, on a Form W-9 (or other acceptable substitute) required by this section.

(2) *Circumstances establishing reasonable reliance.* For purposes of paragraph (e)(1) of this section, a payor can reasonably rely on a Form W-9 (or other acceptable substitute) unless—

(i) The form does not contain the name and taxpayer identification number of the payee (or does not state, in lieu of a taxpayer identification number, that the payee is awaiting receipt of a taxpayer identification number (i.e., an awaiting-TIN certificate));

(ii) The form is not signed and dated by the payee;

(iii) The form does not contain the statement, when required, that the payee is not subject to withholding due to notified payee underreporting;

(iv) The payee has deleted the jurat or other similar provisions by which the payee certifies or affirms the correctness of the statements contained on the form; or

(v) For purposes of section 3406(a)(1)(C), the payor is required to subject the account to which the form relates to withholding under section 3406(a)(1)(C) under the circumstances described in §31.3406(c)-1(c)(3)(iii).

CFR. 31.3406(d)-5

Backup withholding when the Service or a broker notifies the payor to withhold because the payee's taxpayer identification number is incorrect.

(a) *Overview.* Backup withholding under section 3406(a)(1)(B) applies to any reportable payment made with respect to an account of a payee if the Internal Revenue Service or a broker notifies a payor under paragraph (c)(1) or (2) of this section that the payee's name and taxpayer identification number combination (name/TIN combination) is incorrect and the payor is required under paragraph (c)(3) of this section to identify that account as having the same name/TIN combination. After receiving a notice from the Internal Revenue Service or a broker under paragraph (c)(1) or (2) of this section and identifying an account as having the incorrect name/TIN combination under paragraph (c)(3) of this section, the payor must notify the payee in accordance with paragraph (d) of this section. In addition, under paragraph (e) of this section, the payor must backup withhold on all reportable payments made to such account after the close of the 30th business day after the date that the payor receives the notice and on or before the close of the 30th calendar day after the date that the payor receives from the payee the certification required under paragraph (f) of this section. Under paragraph (g) of this section, if a payor receives 2 notices from the Internal Revenue Service or broker within 3 calendar years with respect to a payee's account, the payor must notify the payee in accordance with paragraph (g)(2) (rather than paragraph (d)) of this section. In addition, the payor must backup withhold on all reportable payments made with respect to the account after the close of the 30th business day after the date that the payor receives the second notice and on or before the 30th calendar day after the date that the payor receives notification from the Social Security Administration (or the Internal Revenue Service) validating a name/TIN combination for the account. Paragraph (h) of this section requires a payor to use a corrected name/TIN combination on subsequent information returns.

CFR. 31.3406(d)-5(d)

d) *Notice from payors of backup withholding due to an incorrect name/TIN combination* —(1) *In general.* Except as provided in paragraph (g) of this section, if a payor receives notice under paragraph (c)(1) or (2) of this section and is required to identify an account as having the incorrect name/TIN combination under paragraph (c)(3) of this section, the payor must send a copy of the notice (or an acceptable substitute notice) to the payee of the account in accordance with the procedures of paragraph (d)(2) of this section.

CFR. 31.3406(d)-2

Payee certification failure.

(a) *Requirement to backup withhold.* Withholding under section 3406(a)(1)(D) applies to a reportable interest or dividend payment (as defined in section 3406(b)(2)) if, and only if, the payee fails to certify to the payor, under penalties of perjury, that the payee is not subject to withholding due to notified payee underreporting under section 3406(a)(1)(C). The period for which withholding applies is described in §31.3406(e)–1(e). See §31.3406(d)–3(a) for special

rules when an account is established directly with, or an instrument is acquired directly from, the payor by electronic transmission or by mail. See §31.3406(c)–1(c)(3)(iv) for rules with respect to a payor's reliance on a payee certification for a new account following notified payee underreporting. See §31.3406(d)–4 for special rules relating to the acquisition of a readily tradable instrument through a broker. The certificate on which the certification should be made is described in §31.3406(h)–3.

(b) *Exceptions.* Withholding under section 3406(a)(1)(D) and paragraph (a) of this section does not apply to reportable interest or dividend payments (as defined in section 3406(b)(2)) made—

(1) With respect to a pre-1984 account (as defined in §31.3406(d)–1(b)(1));

(2) In a window transaction (as defined in §31.3406(b)(2)–3(b));

(3) With respect to a readily tradable instrument described in §31.3406(d)–1(b)(2)(iv) or §31.3406(d)–4(a)(3); or

(4) During the period and with respect to an account or readily tradable instrument described in §31.3406(d)–3.

CFR. 31.3406(d)-3(c)

(c) *Application to foreign payees.* The rules of paragraphs (a) and (b) of this section also apply to a payee from whom the payor is required to obtain a Form W–8 (or an acceptable substitute) or other evidence of foreign status (pursuant to relevant regulations under an applicable Internal Revenue Code section without regard to the requirement to furnish a taxpayer identifying number, and the certifications described in §§31.3406(d)–1(b)(3) and 31.3406(d)–2), provided the payee represents orally or otherwise, before or at the time of the acquisition or sale of the instrument or the establishment of the account, that the payee is not a United States citizen or resident. The 30-day rules described in paragraph (a) or (b) of this section may apply only if the payee does not qualify for, or the payor does not apply, the 90-day grace period described in §1.6049–5(d)(2)(ii) or §1.1441–1(b)(3)(iv) of this chapter.

CFR. 31.3406(d)-5(f)

(f) *Manner required for payee to furnish certified taxpayer identification number.* (1) Except as provided in paragraph (g) of this section, in order to prevent backup withholding under paragraph (e) of this section from starting, or to stop it once it has begun, a payee with respect to whom the payor has been notified under paragraph (c)(1) or (2) that the payee's name/TIN combination is incorrect is required on Form W–9 (or an acceptable substitute form) to—

(i) Provide the payee's name and taxpayer identification number; and

(ii) Certify, under penalties of perjury, that the taxpayer identification number being provided is correct.

CFR. 31.3406(e)-(2)

(2) *Stop withholding.* The payor must stop withholding under section 3406(a)(1)(A) within 30 days after the payor receives—

- (i) The payee's taxpayer identification number in the manner required under §31.3406(d)-1; or
- (ii) A statement, in such form and containing such information as is required under applicable regulations, that the payee is not a United States person.

(c) *Notification of an incorrect taxpayer identification number.* See §31.3406(d)-5(e) and (g)(3) for the period for which withholding is required in the case of notification of an incorrect taxpayer identification number.

(d) *Notified payee underreporting.* See §31.3406(c)-1(e) for the period for which withholding is required in the case of notified payee underreporting.

(e) *Payee certification failure* —(1) *Start withholding.* A payor is required to withhold under section 3406(a)(1)(D) at a rate of 31 percent on any reportable interest or dividend payment (as defined in section 3406(b)(2)) at the time the payor pays such reportable interest or dividend payment (as described in §31.3406(a)-4) to a payee if—

- (i) The payor has not received from the payee the certification required in §31.3406(d)-2; or
- (ii) The payor has received notice from a broker (as required in §31.3406(d)-4(a)(1)(iii)) with respect to a readily tradable instrument that the payee did not make the required certification and the payor has not received the required certification from the payee.

(2) *Stop withholding.* The payor must stop withholding under section 3406(a)(1)(D) on any reportable interest or dividend payment within 30 days after the payor receives the certification from the payee in the manner required by §31.3406(d)-2.

(f) *Rule for determining when the payor receives a taxpayer identification number or certificate from a payee.* In determining whether a payee has failed to provide a taxpayer identification number or any certification to a payor (including a Form W-8 or substitute form), a payor is required to process the taxpayer identification number or certification within 30 days after the payor receives the taxpayer identification number or certification from the payee or in certain cases, from a broker. Thus, the payor may take up to 30 days to treat the taxpayer identification number or a certificate as having been received.

CFR. 31.3406(c)-1(b)(2)

(2) *Payee underreporting* —(i) *In general.* *Payee underreporting* means that the Internal Revenue Service has determined, for a taxable year, that—

(A) A payee failed to include in the payee's return of tax under chapter 1 of the Internal Revenue Code for that year any portion of a reportable interest or dividend payment required to be shown on that tax return; or

(B) A payee may be required to file a return for that year and to include a reportable interest or dividend payment in the return, but failed to file the return.

(ii) *Payments included in making payee underreporting determination.* The determination of whether there is payee underreporting is made by treating as reportable interest or dividend payments, all payments of dividends reported under section 6042, all patronage dividends reported under section 6044, and all interest and original issue discount reported under section 6049, regardless of whether withholding due to notified payee underreporting applies to those payments.

(c) *Notice to payors regarding backup withholding due to notified payee underreporting* —(1) *In general.* If the Internal Revenue Service or a broker notifies a payor that a payee is subject to withholding due to notified payee underreporting, the payor must—

(i) Identify any accounts of the payee under the rules of paragraph (c)(3) of this section; and

(ii) Notify the payee and withhold under section 3406 on reportable interest or dividend payments made with respect to any identified account under the rules of paragraphs (d) and (e) of this section.

(2) *Additional requirements for payors that are also brokers* —(i) *In general.* A broker must notify the payor of a readily tradable instrument that the payee of the instrument is subject to withholding due to notified payee underreporting if—

(A) The broker (in its capacity as a payor) receives a notice from the Internal Revenue Service under paragraph (c)(1) of this section that a payee is subject to withholding due to notified payee underreporting and the broker is required to identify an account of the payee under paragraph (c)(3) of this section;

(B) The payee subsequently acquires the instrument from the broker through the same account; and

(C) The acquisition of the instrument occurs after the close of the 30th business day after the date that the broker receives the notice (or on any earlier date that the broker may begin applying this paragraph (c)(2) after receipt of the notice described in paragraph (c)(1) of this section).

(ii) *Transfer out of street name.* For purposes of this paragraph (c)(2), an acquisition includes a transfer of an instrument out of street name into the name of the registered owner (i.e., the payee).

(iii) *Method of providing notice.* A broker must provide the notice required under this paragraph (c)(2) to the payor of the instrument with the transfer instructions for the acquisition. See §31.3406(d)-4(a)(2).

(iv) *Termination of obligation to provide information.* The obligation of a broker to provide notice to payors under this paragraph (c)(2) terminates simultaneously with the termination of the broker's obligation to withhold (in its capacity as payor) due to notified payee underreporting on reportable interest or dividends made with respect to the account.

26 USC Sec. 3406(b)(2)

Reportable interest payment.

(a) *Interest subject to backup withholding* —(1) *In general.* A payment of a kind, and to a payee, that is required to be reported under section 6049 (relating to returns regarding interest and original issue discount) is a reportable payment for purposes of section 3406, subject to the special rules of §31.3406(b)(2)-2 (relating to original issue discount) and §31.3406(b)(2)-3 (relating to window transactions). See §31.6051-4 for the requirement to furnish a statement to the payee if tax is withheld under section 3406.

(2) *Special rule for tax-exempt interest.* When an issuer is required to make an information return under §1.6049-4(d)(8) of this chapter because a payee provided a signed written statement on the envelope or shell incorrectly claiming that the interest was exempt from taxation under section 103(a) (as described in §1.6049-5(b)(1)(ii) of this chapter), the issuer is not required to impose withholding under section 3406.

(b) *Amount subject to backup withholding* —(1) *In general.* The amount of interest subject to withholding under section 3406 is the amount subject to reporting under section 6049.

(2) *Special rule to adjust for premature withdrawal penalty.* Solely for purposes of computing the amount subject to withholding under section 3406, the payor may elect not to withhold from the portion of any interest payment that is not received by the payee because a penalty is in fact imposed for premature withdrawal of funds deposited in a time savings account, certificate of deposit, or similar class of deposit.

CFR. 31.3406(c)-1

Notified payee underreporting of reportable interest or dividend payments.

(a) *Overview.* Withholding under section 3406(a)(1)(C) applies to any reportable interest or dividend payment (as defined in section 3406(b)(2)) made with respect to an account of a payee if the Internal Revenue Service or a broker notifies a payor under paragraph (c) (1) or (2) of this section that the payee is subject to withholding due to notified payee underreporting (as defined in paragraph (b)(1) of this section), and the payor is required under paragraph (c)(3) of this section to identify that account. After receiving the notice and identifying accounts, the payor must notify the payee, in accordance with paragraph (d) of this section, that withholding due to

notified payee underreporting has started. Paragraph (e) of this section describes the period for which withholding due to notified payee underreporting is required. Paragraph (f) of this section provides rules concerning notices that the Internal Revenue Service will send to a payee before notifying a payor that the payee is subject to withholding due to notified payee underreporting. Paragraph (g) of this section provides rules that a payee can use to prevent withholding due to notified payee underreporting from starting or to stop it once it has started. Paragraph (h) of this section provides special rules for joint accounts of payees who have filed a joint return. See section 6682 for the penalties that may apply to a payee subject to withholding under section 3406(a)(1)(C).

CFR. 31.3406(c)-1(g)(1)

(g) Determination by the Internal Revenue Service that backup withholding should not start or should be stopped —(1) *In general.* A payee may prevent withholding due to notified payee underreporting from starting, or stop the withholding once it has started, by requesting and receiving a determination from the Internal Revenue Service under one or more of the provisions of paragraph (g)(3) of this section. Following its review of a request for a determination under paragraph (g)(3) of this section, the Internal Revenue Service will either make the determination or provide the payee with a written report informing the payee that the request for determination is being denied and the reasons for the denial. If a determination is made during the notice period (as defined in paragraph (f)(1) of this section), the payee is not subject to withholding due to notified payee underreporting with respect to any taxable year for which a determination was made. If a determination is made after the notice period, the Internal Revenue Service will, at the time prescribed in paragraph (g)(2) of this section, provide written certification to a payee that withholding is to stop, and will notify payors who were contacted pursuant to paragraph (c)(1) of this section to stop withholding. A broker who (in its capacity as payor) under this paragraph (g)(1) receives a notice from the Internal Revenue Service or a copy of the certification provided to a payee by the Internal Revenue Service is not required to provide a corresponding notice to any payors whom the broker has previously notified under paragraph (c)(2) of this section.

CFR. 31.3406(c)-1(g)(3)

(3) Grounds for determination. The Internal Revenue Service will make a determination that withholding due to notified payee underreporting should not start or should stop once it has started if the payee—

(i) Shows that there was no payee underreporting (as provided in paragraph (g)(4) of this section) for each taxable year with respect to which the Internal Revenue Service determined under paragraph (b)(2) of this section that there was payee underreporting;

(ii) Corrects any payee underreporting (as provided in paragraph (g)(5) of this section) for each taxable year with respect to which the Internal Revenue Service determined under paragraph (b)(2) of this section that there was payee underreporting;

(iii) Shows that withholding will cause or is causing an undue hardship (as defined in paragraph (g)(6) of this section) and that it is unlikely that the payee will underreport interest or dividend payments again; or

(iv) Shows that a bona fide dispute exists regarding whether any underreporting has occurred (as provided in paragraph (g)(7) of this section) for each taxable year with respect to which the Internal Revenue Service determined under paragraph (b)(2) of this section that there was payee underreporting.

CFR. 31.3406(c)-1(f)(1)

(f) Notice to payees from the Internal Revenue Service —(1) Notice period. After the Internal Revenue Service determines under paragraph (b)(2) of this section that payee underreporting exists, the Internal Revenue Service will mail to the payee at least four notices over a period of at least 120 days (the notice period) before payors will be notified under paragraph (c)(1) of this section that the payee is subject to withholding due to notified payee underreporting. The notices may be accompanied by, or incorporated in, other notices provided to the payee by the Internal Revenue Service.

CFR. 31.3406(c)-1(f)(2)

(2) Payee subject to backup withholding. After the Internal Revenue Service provides the notices described in paragraph (f)(1) of this section, the Internal Revenue Service will send notices to payors under paragraph (c)(1) of this section unless—

(i) A payee obtains a determination under paragraph (g) of this section; or

(ii) In the case of a payee who has filed a tax return, the Internal Revenue Service has not assessed the deficiency attributable to the underreporting.