

April 2017

## Private Foundations Bulletin

# Vendor Tax Compliance: What You Need To Know

We recently received an increasing number of inquiries regarding tax compliance with respect to payments to vendors — and, especially, foreign vendors. The tax compliance surrounding the use of foreign vendors can be complex and should be understood by management before entering into such arrangements.

This bulletin aims to simplify the process of determining:

- the type of tax documentation that should be acquired from a vendor at the point of engagement,
- whether or not a vendor should receive a form/have taxes withheld,
- the filing thresholds of each form, and
- the due date of each form.

Depending on the type of vendor, the services being provided, and where the work is being performed, the foundation would file either a federal **Form 1099-MISC**, *Miscellaneous Income*, a federal **Form 1042-S**, *Foreign Person's U.S. Source Income Subject to Withholding*, or, in some cases, neither of the two depending on the circumstances. These forms detail the total dollar amount of income paid during the calendar year to the vendor, along with information regarding any tax withholdings that might have been remitted to United States tax authorities.

## Obtaining Proper Documentation from Vendors

Typically, at the start of a vendor arrangement, various documents (signed contract, payment instructions, certificate of insurance, etc.) are obtained from the vendor to initiate the relationship. However, an item that is often overlooked is the vendor's tax status form.

For U.S. tax domiciled vendors, federal **Form W-9**, *Request for Taxpayer Identification Number and Certification*, should be requested. As for foreign tax domiciled vendors, one of two forms should be requested: federal **Form W-8BEN**, *Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Individuals)*, or, for non-individuals, federal **Form W-8BEN-E**, *Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities)*.

## Useful Tips When Determining Whether a Vendor Should Receive a Form or Whether Tax Withholding Should Occur

Once the proper tax status form (**W-9**, **W-8BEN** or **W-8BEN-E**) has been obtained and analyzed by the foundation, a determination can be made if the vendor should receive a **Form 1099-MISC**, **Form 1042-S** or nothing at the end of the year and whether or not any United States tax withholdings should occur at the time of payment.

## U.S. Tax Based Entities

Upon obtaining **Form W-9** for United States tax based entities, line 3 of the form should be reviewed to determine the federal tax classification of the vendor. Vendors that have checked either box "C - Corporation" or "Limited Liability Company with a tax classification of C" are not required to receive a **Form 1099**. All other vendors should receive **Form 1099-MISC**, with limited exceptions.

## Foreign-Based Taxing Entities

The compliance rules regarding foreign-based taxing entities are often complex as the rules differ depending on the taxing country of the vendor, where services are performed, as well as the United States tax treaty with that particular country. As a general rule, all foreign-based taxing entities that have performed services in the United States should receive a **Form 1042-S**, subject to limited exceptions due to country-specific tax treaties and rules. If the foreign-based vendor has performed services outside of the United States, it is then likely that a **Form 1042-S** is not required, and there is no further filing requirements.

For those foreign vendors that do perform services in the United States, income reporting thresholds and tax withholding rates are country specific, making the process of determining whether withholding should occur challenging. Part II of **Form W-8BEN** and Part III of **Form W-8BEN-E** detail the tax treaty benefits being claimed by the vendor under the specific tax treaty between the United States and the country in question. The specific article and paragraph of the treaty, along with the withholding tax rate as indicated in the treaty, should be identified. However, the dollar threshold that triggers withholdings to occur is not included on these forms.

In the event that a withholding payment is required, it should be remitted to the United States government (either by check or EFTPS) at the time of withholding. Consultation with a tax expert who is familiar with the various United States tax treaties is one way in which a private foundation can determine whether they have met the thresholds to trigger withholdings.

## **Filing Thresholds – 1099-MISC and 1042-S**

For United States based taxing entities, some of the most common items that can cause a private foundation to file **Form 1099-MISC** are as follows:

- Rents (reported in Box 1) of at least \$600
- Other income payments (reported in Box 3) of at least \$600
- Prizes and awards (reported in either Box 3 or 7 depending on circumstances) of at least \$600
- Medical and health care payments (reported in Box 6) of at least \$600
- Services performed by someone who is not your employee (reported in Box 7) of at least \$600, including parts and materials
- Royalties or broker payments in lieu of dividends or tax-exempt interest (reported in Box 8) of at least \$10

Depending on whether the vendor is a United States or foreign-based taxing entity, differing reporting requirements will apply. For foreign-based taxing entities, there is generally no dollar threshold to file a **Form 1042-S**.

## **Due Dates**

Under current Internal Revenue Service filing requirements, in any given year, federal **Form 1099-MISC** is due on January 31<sup>st</sup> and federal **Form 1042-S** is due on March 15<sup>th</sup>. Extensions do exist, if timely filed forms are submitted. It should be noted that a private foundation's fiscal year-end does not affect the timing of the due dates indicated above.

## Contact Us

Should you have any questions regarding your private foundation's compliance with any of the items detailed in this bulletin, please contact the following experienced professionals in our Philanthropic and Private Foundation Services Practice: Thomas F. Blaney, CPA, CFE, Partner and Co-Director at [tblaney@pkfod.com](mailto:tblaney@pkfod.com) or Christopher D. Petermann, CPA, Partner and Co-Director at [cpetermann@pkfod.com](mailto:cpetermann@pkfod.com).

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