

MEMO# 15443

December 12, 2002

IRS ISSUES FINAL REGULATIONS PROVIDING EXPEDITED PROCESS TO OBTAIN INDIVIDUAL TAXPAYER IDENTIFICATION NUMBERS FOR FOREIGN PAYEES

[15443] December 12, 2002 TO: PENSION MEMBERS No. 59-02 PENSION OPERATIONS ADVISORY COMMITTEE No. 82-02 TAX MEMBERS No. 51-02 RE: IRS ISSUES FINAL REGULATIONS PROVIDING EXPEDITED PROCESS TO OBTAIN INDIVIDUAL TAXPAYER IDENTIFICATION NUMBERS FOR FOREIGN PAYEES The Internal Revenue Service ("Service") has issued the attached final regulations, under Sections 1441 and 6109 of the Internal Revenue Code, that provide procedures pursuant to which withholding agents may assist foreign individuals receiving certain "unexpected payments" in obtaining the benefit of reduced rates of US withholding tax provided under an income tax treaty. Specifically, in situations where the individual receiving the unexpected payment has not documented in advance eligibility for the treaty benefit, the regulations generally permit withholding agents (1) to obtain an individual taxpayer identification number ("ITIN") for the individual on an expedited basis and (2) to rely, in certain cases, on a Form W- 8BEN ("Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding") without an ITIN to withhold tax at the lower treaty rate.¹ The scope of these regulations is narrow in that they are limited to "unexpected payments." Thus, they may apply to certain distributions from qualified plans, annuities or individual retirement accounts to foreign individuals.² The regulations do not apply generally to dividends paid by US mutual funds, as foreign individuals are not required to provide an ITIN to claim reduced rates of US withholding tax on mutual fund dividends under an income tax treaty.³ Two suggestions made by the Institute,⁴ when these regulations were issued in 1 Generally, a foreign individual must provide a withholding agent with an IRS Form W-8BEN (that includes an ITIN) in advance of a payment for which treaty benefits will be claimed. 2 For example, it may be necessary to obtain an ITIN on an expedited basis for payment of a death benefit to a foreign individual. 3 See Treas. Reg. 1.1441-6(c)(2). 4 See Institute Memorandum to Pension Members No. 16-02, Pension Operations Advisory Committee No. 24-02, and Tax Members No. 21-02, dated April 18, 2002. 2 temporary and proposed form earlier this year,⁵ were not adopted.⁶ First, we recommended that the beneficiaries be permitted to claim treaty benefits without providing an ITIN to the withholding agent on Form W-8BEN. The death benefit is wholly unrelated to any activities of the foreign individual within the United States and, given the inability of the foreign individual to control the timing of his or her entitlement to the distribution, the death benefit also is functionally equivalent to a distribution with respect to

a publicly-traded security for which an exemption from the ITIN requirement exists under current Treasury regulations. Second, we recommended that where a foreign individual receiving a death benefit from a U.S. retirement plan does provide an ITIN on Form W-8BEN when claiming treaty benefits, the Form W-8BEN be permitted to remain valid indefinitely, regardless of whether a distribution is made and reported to the foreign individual on Form 1042-S (“Foreign Person’s U.S. Source Income Subject to Withholding”) for each consecutive year.⁷ The consecutive distribution rule creates a classic and confusing “trap for the unwary” for withholding agents that potentially could be required to resolicit Forms W-8BEN from foreign beneficiaries on an ad hoc basis. The administrative burdens of the consecutive distribution rule appear to outweigh its benefits, given that a foreign beneficiary already is required to provide a withholding agent with notice of any change in circumstances that would invalidate a previously submitted Form W-8BEN. Catherine Barré

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5 See Institute Memorandum to Pension Members No. 3-02, Pension Operations Advisory Committee No. 5-02, and Tax Members No. 4-02, dated January 24, 2002. 6 The Service adopted the Temporary and Proposed Regulations as final without revision. 7 Current Treasury regulations provide that a Form W-8BEN with an ITIN may remain valid indefinitely, provided that the withholding agent reports at least one payment annually to the beneficial owner on Form 1042-S or the ITIN otherwise is provided by the withholding agent to the IRS (the “consecutive distribution” rule). Treas. Reg. 1.1441-1(e)(4)(ii)(B).