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IRS to Audit Employers Sponsoring H-1B Visa Holders

The Internal Revenue Service (IRS) recently announced that it will start conducting audits of withholding agents related to payments made to nonresident foreign nationals as a "Tier 1" issue. These audits may be mandatory for certain employers sponsoring foreign nationals working in the United States on H-1B visas. Therefore, all such employers who are audited by the IRS's Large and Mid-size Business (LMSB) Division can expect to have inspected their reporting (Forms 1042 & 1042-S) and withholding obligations under IRC 1441.

The IRS's description of this issue is available here:

<http://www.irs.gov/businesses/corporations/article/0,,id=205415,00.html>.

Background

Generally, U.S. persons who make fixed, determinable, annual or periodic (FDAP) payments to nonresident aliens are required to withhold 30 percent (or a lesser rate under an applicable treaty) and to file an annual return (Form 1042) and to issue a statement to the payee (Form 1042-S). The payer is a withholding agent who can be held personally liable for failure to withhold.

A "Tier 1" designation means this issue is one of high strategic importance to LMSB and may have significant impact on one or more industries. These issues are coordinated and subject to mandatory audit procedures.

The H-1B nonimmigrant visa category is granted to foreign nationals who will be employed temporarily by a U.S. employer in professional positions that qualify as specialty occupations. The H-1B petition process requires that a U.S.

employer file a petition on behalf of the foreign national for whom they are seeking H-1B classification. As part of the petition, the U.S. employer must make attestations to the Department of Labor including that it will pay the H-1B



employee the required wage and that it will provide working conditions to the H-1B employees that will not adversely affect other workers similarly employed. In addition to these attestations, the U.S. employer is responsible for properly reporting income earned and withholdings made to the H-1B employees.

Current Initiative

The IRS will focus on the quality of the overall reporting and withholding systems and procedures of the withholding agents to ensure proper classification of payments, sourcing, and the validity of documentation of foreign nationals. This could include a review of the information submitted to and retained by the withholding agent to justify the reporting and withholding (e.g., Form W-8 BEN).

The failures of the withholding agent to report and to withhold may lead to personal liability and to penalties. The discovery of fraudulent activities related to obtaining or maintaining the H-1B can also lead to severe immigration penalties, including permanently barring the U.S. employer from participating in the H-1B program.

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