Tax Law Update

December 14, 2010

New Withholding Requirements

- ***Tax Increase Prevention and Reconciliation Act of 2005*** **created subsection 3402(t) of the IRC**
- **Subsection 3402(t) mandated 3% federal tax withholding on payments made by government entities**
- **Applied to payments for both goods and services made after December 31, 2010**
- ***The American Recovery and Reinvestment Act of 2009*** **delayed 3% withholding for one year, until after December 31, 2011**

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Governmental Entities Required to Withhold

- The entire US government
- All states, including DC (but not tribal governments)
- All political subdivisions and instrumentalities of a State government (unless annual payments for goods and services are less than $100 million per year)

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Payment Threshold

- Payments made by government or its payment administrator of $10,000 or more
- Multiple payments do not have to be aggregated unless abuse present
- Anti-abuse rules require aggregation if purpose of multiple payments is to avoid 3402(t) rules

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Payment Administrator

Payment administrator is any person that acts as an agent for a government entity. Transfers to the payment administrator are exempt, but payments of fees are subject.

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Credit Card Payments

Payments made by credit cards and procurement cards are subject to 3% withholding at the point of sale, not when government makes payment to the bank. Governmental entity remains liable for withholding and reporting associated with payment.

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Payments Exempt From Withholding

- Wage payments to employees
- Payments subject to backup withholding
- Interest payments
- Payments for real property
- Payments to other governments, tax-exempt entities
- Classified contracts (IRC 6050M)
- Payments by a political subdivision which annually makes payments of less than $100 million
- Payments for public assistance or public welfare that is determined on a needs or income basis

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Payments Exempt From Withholding (Continued)

- Travel reimbursements to governmental employees, transfers to pension funds
- Other payments such as social security benefits, unemployment compensation, emergency or disaster payments, CCC loans, payments of annuities to individuals, payments to NRAs exempt due to treaty

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Persons Subject to Withholding Under IRC 3402(t)

- Individuals
- Trusts
- Estates
- Partnerships
- Associations
- Companies
- Corporations

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Depositing and Reporting Amounts Withheld Under 3402(t)

- Use Form 945, Annual Return for Withheld Federal Income Tax
- Report amounts to recipients on Form 1099-MISC

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Effective Date and Transition Relief for Existing Contracts

- **Effective for payments made after December 31, 2011**
- **Contracts already in existence are exempt unless substantially modified subsequent to effective date**

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The Patient Protection and Affordable Care Act of 2010

- **Payments of $600 or more made to corporations must be reported on Form 1099, beginning January 1, 2012.**
- **Amounts paid for both property and services must be reported on Form 1099.**

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Exemptions from Expanded Reporting Requirements

- **Governments and non-profits continue to be exempt from receiving Forms 1099**
- **Payment Cards and Third Party Networks subject to IRC 6050W Reporting will be exempt from expanded reporting**
- **IRS to issue other rules designed to avoid duplicate reporting**

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