Internal Revenue Service
DEPARTMENT OF THE TREASURY

LB&I Process Unit

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Process Overview

Adjustments for Overwithholding on Form 1042

This Unit discusses adjustments for overwithholding of tax done on payments of U.S. source income to foreign persons on Forms 1042 tax returns and Forms 1042-S information returns. For discussions on correct withholding, see the "Related Practice Units" slide at the end of this Unit.

Overwithholding can result from an error or may have been correct based on the documentation available at the time the tax was withheld.

Withholding Agents (WAs) may make limited adjustments or claim a credit for certain overpayments of tax on income withheld from nonresident aliens and foreign corporations.

WAs can always correct the reporting of the withholding they applied. They usually must make reporting corrections of which they are aware.

Detailed Explanation of the Process

Adjustments for Overwithholding on Form 1042
Analysis

How corrections to overwithholding are made depends on whether the overwithholding is discovered: (1) before last deposits for the year, (2) before Form 1042-S due date (with additional limitations), or (3) after that.
 	
1. A WA that discovers overwithholding before the WA's final deposits are made for the year can make balancing payments to the payees and to the IRS. In this case the WA never needs to report the errors or corrections to the IRS.
2. A WA that has overwithheld and already completed its deposits for the calendar year but whose Forms 1042-S have neither been sent out nor are overdue, may adjust the overwithheld amount using one of the following methods:
  a. Reimbursement Procedure (Treas. Reg. 1.1461-2(a)(2)) or,
  b. Set-off Procedure (Treas. Reg. 1.1461-2(a)(3)).
3. A WA that discovers overwithholding after the earlier of (a) the due date of Forms 1042-S, including extensions that have been granted, or (b) the date WA has provided a Form 1042-S to either Beneficial Owner (BO) or the IRS, must report the overwithholding on Form 1042-S and the recipient must claim a refund for the overwithholding. Proposed burden reduction regulations 132881-17 anticipate that the expanded time allowed for reimbursement and set-off corresponding to any granted extensions of time to file Forms 1042-S will be effective for 2019 calendar year.

Step 1: Overwithholding Fixed Before the Last Deposit

Adjustments for Overwithholding on Form 1042

Step 1

Overwithholding discovered and corrected before the last deposits for the year are due.

Considerations	Resources
Overwithholding could occur for many reasons. Most commonly, it seems to occur because a payee has not supplied complete documentation that allows a WA to withhold less than 30%. If the reason for overwithholding is rectified and the WA would like to correct the overwithholding before the last deposit for the year has been made, the WA may do so by repaying the payee that was overwithheld upon and reducing deposits associated with payments to be made later in the same calendar year. The WA reports on Forms 1042-S to all of the payees without noting the overwithholding that has already been corrected. Dates that final deposits are due:	▪ Pub. 515 - *Withholding of Tax on Nonresident Aliens and Foreign Entities* ▪ Form 1042 Instructions

Liability Amount	Last Deposit Due
$2,000 or more	3 business days after 12/31/x1
$200 or more but less than $2,000	3/15/x2
Less than $200	Later of 3/15/x2 and Form 1042 filing date

On lines 1-60 of Form 1042, the WA's liability is the higher one until the reason for overwithholding is corrected.

See Example #1

Step 2: Overwithholding Fixed Using Reimbursement

Adjustments for Overwithholding on Form 1042

Step 2

For overwithholding discovered soon enough, but after deposits were complete, the WA repays the payee by not making deposits that are due for year 2. WA must show the overwithholding and correction on Forms 1042-S and Form 1042.

Considerations	Resources
▪ When overwithholding to BO1 in 2018 is to be corrected between 1/1/2019 and the due date of Forms 1042-S (including extensions), a WA may use the reimbursement procedures. **!** **CAUTION:** In addition to the Form 1042-S due date (including any extensions) cutoff, these procedures can only be used before the first Form 1042-S is sent to either BO1 or the IRS. ▪ WA repays BO1 by NOT depositing funds it would have had to deposit for other payees (BO2 and BO3) in 2019. BO2 and BO3 are withheld upon correctly but WA does not deposit some of the funds. ▪ WA shows on BO1's 1042-S for 2018 the high dollar withholding in box 7a and a repayment in box 9 (per the new box numbering on Form 1042-S for 2018) such that the total withholding credit (TWC) available to the BO in box 10 is correct, based on the gross income and the corrected tax rate of box 3b. **!** **CAUTION:** The examples in this Unit pertain to Forms 1042-S up to 2017. The 2018 form switched the position of boxes 9 and 11 to result in a more logical intermediate step calculation of BO's "Total withholding credit" on Box 10. In this practice unit we refer to Form 1042-S box numbering using 2018 numbering.	▪ Treas. Reg. 1.1461-2(a)(2) ▪ Form 1042 Instructions ▪ Form 1042-S Instructions

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Adjustments for Overwithholding on Form 1042

Step 2

Considerations	Resources
• WA has deposited more during 2018 than it now knows that it should have. Therefore WA shows the high deposits on Form 1042, and gets a credit usable on the 2019 Form 1042, because the 2018 deposits exceed the corrected lower liability for 2018. • If this was the only correction, all of the Forms 1042-S for 2019 (Year 2) appear entirely normal. • Form 1042 for 2019 shows fewer deposits in 2019 relative to the liabilities shown on all of the 2019 Forms 1042-S, and this exactly uses up the credit that was shown on the 2018 Form 1042. See Example #2	

Adjustments for Overwithholding on Form 1042

Step 2

Considerations	Resources

Stated another way:
 	
For 2018 (Year 1):
 	
A WA may only reduce a deposit of tax otherwise due for a 2019 payment for the overwithholding in 2018 if WA:
 	
1. On the 2018 Form 1042-S (timely filed, now including extensions):
   a) Puts the dollar amount of federal tax withheld during 2018 (box 7a),
   b) Puts the amount repaid to recipient (in early 2019) (box 9),
   c) Puts the total withholding credit is box 7a plus box 8 less box 9 and
   d) Puts the corrected lower tax rate in box 3b.
2. On the 2018 Form 1042 (timely filed, now including extensions):
   a) Puts the amount WA repaid to BO1 on line 63c(1) and 70a,
   b) Checks the credit box on line 71,
   c) Includes the total 2018 overwithheld dollar amounts on lines 63a and 65a,
   d) Includes the net (after repaying BO1) liability amount on lines 63e, 64b and 64e,
   e) Adjusts liability of line 59 (or a prior quarter monthly period, if necessary to avoid negative liability) by the repaid amount.
	▪ Treas. Reg. 1.6414-1

Adjustments for Overwithholding on Form 1042

Step 2

Considerations	Resources

For 2019 (Year 2):
 	
A WA that reduces a deposit of tax otherwise due for a 2019 payment for overwithholding done in 2018 should report on its 2019:
 	
1. Forms 1042-S:
    a) All have full dollar withholding (box 7a) and the full tax rate (box 3b). Repaid amounts of box 9 is blank. That is, no unusual entries are required.
 	
2. Form 1042:
    a) Reports the full 2019 tax liability on lines 1 through 60 and lines 64b and 64e.
    b) Reduces the amount deposited on line 65a by the 2018 overwithholding.
    c) Includes the overwithholding credit (from 2018 lines 70a and 71) on line 66.
 	
(!) CAUTION: This Practice Unit uses chapter 3 withholding on FDAP income for its examples and explanations. The same procedures and limitations apply to any overwithholding under chapter 4 FATCA regulations.	

Adjustments for Overwithholding on Form 1042

[Step 2](#)

Considerations	Resources
Back to 2018 (Year 1) Form 1042 lines 1-60: ▪ WA's liability for withholding was high before the end of 2018 (year 1), either because BO1's documentation was incomplete, or WA thought it was incomplete. Either way between 1/1/2019 and 3/15/2019, the 2018 liability was discovered to drop. ▪ To have the 2018 Form 1042 result in the expected credit, that will get used to make up for the reduced deposits of 2019, the recently realized lower liability must be shown for 2018. ▪ WA shows the higher liability on Form 1042 lines 1 to 58, from the week of overwithholding in 2018 until almost the end of 2018. ▪ WA reduces the liability at year end 2018 first on line 59, but not below zero. If line 59 is too small to accommodate the discovered overwithholding, WA reduces line 58, then line 57, and so on. ▪ The WA "shall keep as part of its records a receipt showing the date and amount of any repayment under reimbursement procedures, and provide a copy of such receipt to the BO. For this purpose, a canceled check or an entry in a monthly statement is sufficient provided that the check or statement contains a specific notation that it is a "refund of tax overwithheld."	▪ Treas. Reg. 1.1461-2(a)(2) ▪ Form 1042 Instructions ▪ Form 1042-S Instructions ▪ Treas. Reg. 1.1464-1(b)

Step 2: Overwithholding Fixed Using Reimbursement (cont'd)

Adjustments for Overwithholding on Form 1042

Step 2

Considerations	Resources
⚠️ **CAUTION**: After a WA repays a BO (or reduces 20x2 withholding on the BO in the case of set-off), the amount repaid to the BO per 20x1 Form 1042-S Box 11 is no longer considered to be tax that was actually withheld from the BO, and the BO would not be allowed a refund of that overwithheld amount. Stated another way, a BO's "Total withholding credit" is reduced by the "amount repaid" Additionally, the IRS would not allow a refund to the WA if the WA has issued a Form 1042-S to either the IRS or the BO that indicates the WA withheld from the BO.	▪ Treas. Reg. 1.1464-1(b) ▪ Treas. Reg. 1.1464-1(a) ▪ Treas. Reg. 1.6414-1(c) ▪ Treas. Reg. 1.1461-2(a)(2)(A)

Step 3: Overwithholding Fixed Using Set-off

Adjustments for Overwithholding on Form 1042
Step 3
The set-off procedures correct overwithholding in year 1 by reducing the otherwise required withholding on the same payee in year 2.

Considerations	Resources
▪ The set-off procedure achieves the same purpose and follows nearly identical rules as the reimbursement procedure. ▪ The set-off procedure is reflected in reporting on Forms 1042-S and 1042 for both Year 1 and Year 2 in the same way as the reimbursement procedure. This began in 2016. ▪ The only difference between the two procedures is that the Year 2 payee, BO4, whose withholding is not deposited must be the same payee, BO4 who was overwithheld upon in the prior year. So set-off is only possible for a WA to use if WA would have had to withhold from a payment to BO4 in Year 2. ▪ A receipt from WA to BO4, and a notation of the set-off on WA's Form 1042-S and any statement to BO4 as well as recording in WA's books, is required, as it is under the reimbursement procedures, to notify BO4 as to the overwithholding that occurred in Year 1. BO4 also sees the repayment of the overwithholding on box 9 of the 2018 Form 1042-S. Use of box 9 began in 2016. ▪ The liability reduction in the last period of Year 1 as recorded in line 59 (typically) of Form 1042 is the same as in the reimbursement procedure. ▪ See Example #3	▪ Treas. Reg. 1.1461-2(a)(3) ▪ Form 1042 Instructions ▪ Form 1042-S Instructions

Examples of the Process

Adjustments for Overwithholding on Form 1042
Description
Example #1: Overwithholding fixed before last deposit. Example #2: Overwithholding fixed using reimbursement procedures. Example #3: Overwithholding fixed using set-off procedures. The taxpayer and business names and other identifying information shown in this material are hypothetical. They were chosen from Document 13324 - *Category Lists of Names for Fictionalizing Taxpayer Names and Addresses*.

Adjustments for Overwithholding on Form 1042

Description

#1a Overwithholding Fixed Before Last Deposit

Facts:
- "A" opened an account at Otter Fund in early 2016.
- Otter Fund paid a $10,000 dividend to "A" on 11/1/2016.
- "A" furnished a valid Form W-8BEN-E on 11/8/16.
- Otter Fund paid a $50,000 dividend payment on 11/16/16.

USWA
Otter Fund

$10,000 Dividend
$3,000 WH 11/1/2016 30%

$50,000 Dividend
$6,000 WH, 11/16/2016, 12%

1042-S Totals: $60,000 Dividend
$9,000 WH, 12/31/2016, 15%

FC

"A"
Recipient
Beneficial Owner, or
Payee

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Adjustments for Overwithholding on Form 1042

Description

#1b Overwithholding Fixed Before Last Deposit

Resolution
Otter Fund received a W-8BEN-E from "A" on 11/8/2016, that claimed a 15% treaty rate on dividends. Otter may use a netting adjustment for the earlier overwithholding of $1,500 because:
- An additional payment of the same income type was made to the same foreign person.
- A lower withholding rate was determined to be usable by Otter.
- The availability of the lower rate was discovered before last deposit was due for the year.
- Remaining deposits were sufficient to absorb the earlier overwithholding.

The liability listed on 2016 Form 1042 line 51 should be $3,000, not $1,500, as is shown on example #1c. The liability on line 52 should be $6,000 ($7,500 -$1,500). Line 55, the total liability is $9,000. Because line 51 was greater than $2,000, Otter had to deposit 30% within 3 business days of the first payment, until "A" was documented to be entitled to a lower withholding rate.
The Form 1042-S to "A" shows no overwithholding. It only shows the correct totals for the year.

! **CAUTION:** Setup and coding of new accounts, or "on-boarding" is often the most problematic time for account documentation. Though the deposit dates for one account are usually not visible on Form 1042 due to many other accounts receiving payments, an inquiring auditor comparing the first payment date of a new account to the date on its Form W-8BEN might check for the correct initial liability.

After a grace period, "A" must add an affidavit to his late W-8BEN-E that states that the facts on it were correct back to the date that the first payment was made.

Adjustments for Overwithholding on Form 1042

Description

#1c Overwithholding Fixed Before Last Deposit

Section 1 — Record of Federal Tax Liability (Do not show federal tax deposits here)

Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)	Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)	Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)
1	Jan.	7		21	May	7		41	Sept.	7	
2		15		22		15		42		15	
3		22		23		22		43		22	
4		31		24		31		44		30	
5	Jan. total			25	May total			45	Sept. total		
6	Feb.	7		26	June	7		46	Oct.	7	
7		15		27		15		47		15	
8		22		28		22		48		22	
9		29		29		30		49		31	
10	Feb. total			30	June total			50	Oct. total		
11	Mar.	7		31	July	7		51	Nov.	7	3,000
12		15		32		15		52		15	6,000
13		22		33		22		53		22	
14		31		34		31		54		30	
15	Mar. total			35	July total			55	Nov. total		9,000
16	Apr.	7		36	Aug.	7		56	Dec.	7	
17		15		37		15		57		15	
18		22		38		22		58		22	
19		30		39		31		59		31	
20	Apr. total			40	Aug. total			60	Dec. total		

Annotations at right: 3,000 — 30%; 6,000 — 12%; 9,000 — 15%

61	No. of Forms 1042-S filed: a On paper	b Electronically		1
62	Total gross amounts reported on all Forms 1042-S and 1000:			
a	Total U.S. source FDAP income (other than U.S. source substitute payments) reported		62a	60,000
b	Total U.S. source substitute payments reported:			
	(1) Total U.S. source substitute dividend payments reported		62b(1)	
	(2) Total U.S. source substitute payments reported other than substitute dividend payments . . .		62b(2)	
c	**Total gross amounts reported** (Add lines 62a-b)		62c	60,000
d	Enter gross amounts actually paid if different from gross amounts reported		62d	

Examples of the Process (cont'd)

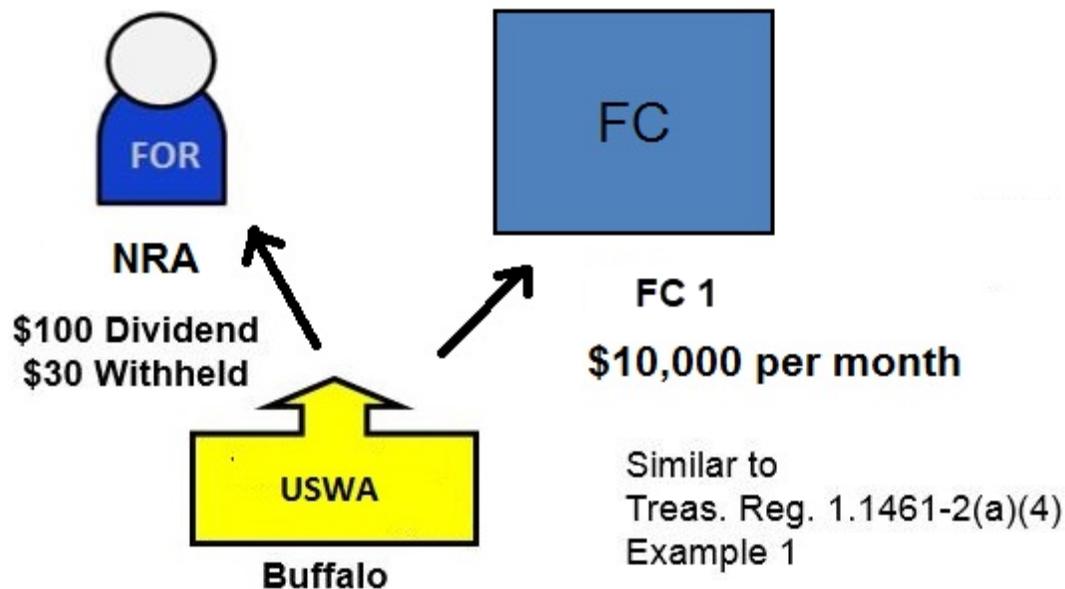| Adjustments for Overwithholding on Form 1042 |
|---|
| **Description** |

#2a Overwithholding Fixed Using Reimbursement Procedures

Facts
In February 2016, NRA, an Indian nonresident alien opened an account at Buffalo Brokerage, "Buffalo". On October 10, 2016, Buffalo paid a one-time $100 dividend to NRA, and withholds $30. NRA receives $70.
Buffalo also pays $10,000 on the first day of each month to FC 1 through all of 2016 and 2017. Buffalo deposits $3,000 per month to the IRS on behalf of FC 1.

NRA
$100 Dividend
$30 Withheld

USWA
Buffalo

FC
FC 1
$10,000 per month

Similar to
Treas. Reg. 1.1461-2(a)(4)
Example 1

Examples of the Process (cont'd)

Adjustments for Overwithholding on Form 1042
Description
#2b Overwithholding Fixed Using Reimbursement Procedures

Resolution
On February 10, 2017 (before Forms 1042-S or 1042 were filed), NRA finally furnished a valid Form W-8BEN to claim the reduced tax rate of 25% under the U.S.-India Income Tax Treaty.

Amount Withheld and Deposited	$30
Withholding Tax Liability	25
Repayment to NRA on 2/10/17	$5

$5 repayment from Buffalo to NRA must be recorded in Buffalo's books

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Examples of the Process (cont'd)

Adjustments for Overwithholding on Form 1042
Description
#2c Overwithholding Fixed Using Reimbursement Procedures Resolution (cont'd) ▪ On March 1, 2017, Buffalo withholds as usual on FC 1 (no change to the liability), but Buffalo reduces the $3,000 deposit to the IRS that Buffalo would normally have made on March 4, 2017, by $5. ▪ #2d shows the 2016 Form 1042-S to NRA. ▪ #2e & #2f show the 2016 Form 1042 filed by Buffalo. ▪ Buffalo used the reimbursement procedures to repay NRA. Because Buffalo made no payments to NRA in 2017, it could not do the repayment to NRA using the setoff procedures. ▪ The 2017 (year 2) Forms 1042-S using for reimbursement or setoff scenarios do not show any evidence of the use of reimbursement or set-off procedures on the 2016 overwithholding. These are not shown. ▪ #2g shows page 2 of Buffalo's 2017 Form 1042.

Adjustments for Overwithholding on Form 1042

Description

#2d Overwithholding Fixed Using Reimbursement Procedures

Form 1042-S for 2016

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Adjustments for Overwithholding on Form 1042

Description

#2e Overwithholding Fixed Using Reimbursement Procedures

Form 1042 for 2016 Page 1

Section 1 Record of Federal Tax Liability (Do not show federal tax deposits here)

Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)	Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)	Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)
1	Jan.	7	3,000	21	May	7	3,000	41	Sept.	7	3,000
2		15		22		15		42		15	
3		22		23		22		43		22	
4		31		24		31		44		30	
5	Jan. total		3,000	25	May total		3,000	45	Sept. total		3,000
6	Feb.	7	3,000	26	June	7	3,000	46	Oct.	7	3,000
7		15		27		15		47		15	30
8		22		28		22		48		22	
9		29		29		30		49		31	
10	Feb. total		3,000	30	June total		3,000	50	Oct. total		3,030
11	Mar.	7	3,000	31	July	7	3,000	51	Nov.	7	3,000
12		15		32		15		52		15	
13		22		33		22		53		22	
14		31		34		31		54		30	
15	Mar. total		3,000	35	July total		3,000	55	Nov. total		3,000
16	Apr.	7	3,000	36	Aug.	7	3,000	56	Dec.	7	2,995
17		15		37		15		57		15	
18		22		38		22		58		22	
19		30		39		31		59		31	
20	Apr. total		3,000	40	Aug. total		3,000	60	Dec. total		2,995

61	No. of Forms 1042-S filed: a On paper	0	b Electronically	2
62	Total gross amounts reported on all Forms 1042-S and 1000:			
a	Total U.S. source FDAP income (other than U.S. source substitute payments) reported	62a		120,100
b	Total U.S. source substitute payments reported:			
	(1) Total U.S. source substitute dividend payments reported	62b(1)		
	(2) Total U.S. source substitute payments reported other than substitute dividend payments	62b(2)		
c	Total gross amounts reported (Add lines 62a-b)	62c		120,100
d	Enter gross amounts actually paid if different from gross amounts reported	62d		120,100

Instructions say reduce Line 59 liability if repaying a BO after year end (before 3/15/x2). But do not use negative liability amounts. Adjust the next prior positive liability.

Examples of the Process (cont'd)

Adjustments for Overwithholding on Form 1042
Description
#2f Overwithholding Fixed Using Reimbursement Procedures Form 1042 for 2016 Page 2

Form 1042 (2016)   Page **2**

63	Total tax reported as withheld or paid by withholding agent on all Forms 1042-S and 1000:		
a	Tax withheld by withholding agent	63a	36,030
b	Tax withheld by other withholding agents:		
	(1) For payments other than substitute dividends	63b(1)	
	(2) For substitute dividends	63b(2)	
c	Adjustments to withholding:		
	(1) Adjustments to overwithholding	63c(1) (	5)
	(2) Adjustments to underwithholding	63c(2)	
d	Tax paid by withholding agent	63d	
e	**Total tax reported as withheld or paid** (Add lines 63a-d)	63e	36,025
64	Total net tax liability		
a	Adjustments to total net tax liability	64a	
b	Total net tax liability under chapter 3	64b	36,025
c	Total net tax liability under chapter 4	64c	
d	Excise tax on specified federal procurement payments (Total payments made x 2%)	64d	
e	**Total net tax liability** (Add lines 64a-d)	64e	36,025
65	Total paid by electronic funds transfer (or with a request for extension of time to file):		
a	Total paid during calendar year	65a	36,030
b	Total paid during subsequent year	65b	
66	Enter overpayment applied as credit from 2015 Form 1042	66	
67	Credit for amounts withheld by other withholding agents:		
a	For payments other than substitute dividend payments	67a	
b	For substitute dividend payments	67b	
68	**Total payments.** Add lines 65 through 67	68	36,030
69	If line 64e is larger than line 68, enter balance due here	69	
70a	Enter overpayment attributable to overwithholding on U.S. source income of foreign persons	70a	5
b	Enter overpayment attributable to excise tax on specified federal procurement payments	70b	
71	Apply overpayment (sum of lines 70a and 70b) to **(check one)**:		
	☑ Credit on 2017 Form 1042 or ☐ Refund		

Section 2   Reconciliation of Payments of U.S. Source FDAP Income

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Examples of the Process (cont'd)

Adjustments for Overwithholding on Form 1042

Description

#2g Overwithholding Fixed Using Reimbursement Procedures

Form 1042 for 2017 Page 2

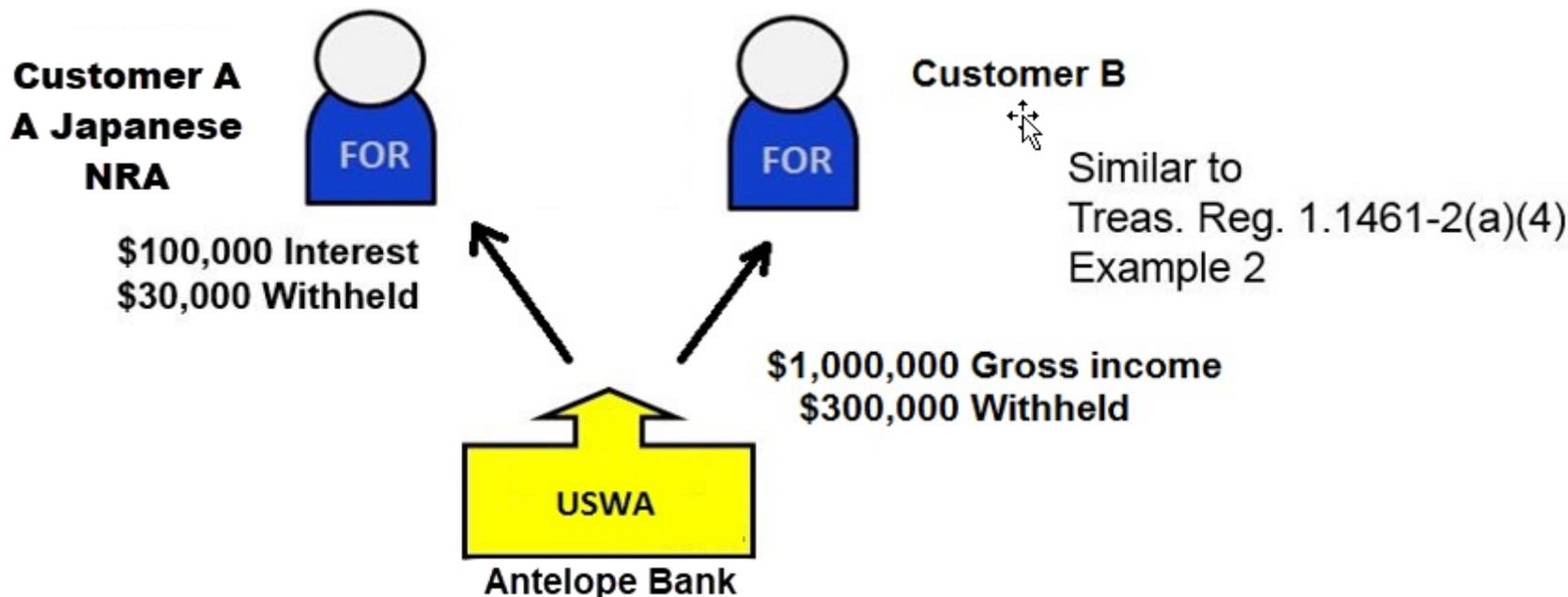|				
63	Total tax reported as withheld or paid by withholding agent on all Forms 1042-S and 1000:			
a	Tax withheld by withholding agent	63a		36,000
b	Tax withheld by other withholding agents:			
	(1) For payments other than substitute dividends	63b(1)		
	(2) For substitute dividends	63b(2)		
c	Adjustments to withholding:			
	(1) Adjustments to overwithholding	63c(1)	(	)
	(2) Adjustments to underwithholding	63c(2)		
d	Tax paid by withholding agent	63d		
e	**Total tax reported as withheld or paid** (Add lines 63a-d)	63e		36,000
64	Total net tax liability			
a	Adjustments to total net tax liability	64a		
b	Total net tax liability under chapter 3	64b		36,000
c	Total net tax liability under chapter 4	64c		
d	Excise tax on specified federal procurement payments (Total payments made x 2%)	64d		
e	**Total net tax liability** (Add lines 64a-d)	64e		36,000
65	Total paid by electronic funds transfer (or with a request for extension of time to file):			
a	Total paid during calendar year	65a		35,995
b	Total paid during subsequent year	65b		
66	Enter overpayment applied as credit from 2016 Form 1042	66		5
67	Credit for amounts withheld by other withholding agents:			
a	For payments other than substitute dividend payments	67a		
b	For substitute dividend payments	67b		
68	**Total payments.** Add lines 65 through 67	68		36,000
69	If line 64e is larger than line 68, enter balance due here	69		
70a	Enter overpayment attributable to overwithholding on U.S. source income of foreign persons	70a		
b	Enter overpayment attributable to excise tax on specified federal procurement payments	70b		
71	Apply overpayment (sum of lines 70a and 70b) to (check one): ☐ Credit on 2018 Form 1042 or ☐ Refund			

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Adjustments for Overwithholding on Form 1042

Description

#3a Overwithholding Fixed Using Set-off Procedures

Facts

In May 2016, Customer A, a Japanese NRA opened an account at Antelope Bank ("Antelope") in Austin, TX but provided no W-8. On September 28, 2016, Antelope made the first $100,000 payment of interest to Customer A on a private note and withheld $30,000. Antelope also pays $1,000,000 and withholds $300,000 on Customer B on December 9, 2016. The next scheduled payment of interest to Customer A is $800,000 on March 10, 2017.

Customer A
A Japanese NRA
FOR

$100,000 Interest
$30,000 Withheld

Customer B
FOR

Similar to
Treas. Reg. 1.1461-2(a)(4)
Example 2

$1,000,000 Gross income
$300,000 Withheld

USWA
Antelope Bank

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Adjustments for Overwithholding on Form 1042
Description

#3b Overwithholding Fixed Using Set-off Procedures
 	
Facts (cont'd)
Customer A furnished a valid Form W-8BEN until February 20, 2017. The March 10, 2017 interest payment to Customer B also does not qualify for the portfolio interest exemption.
 	
Resolution
▪ The U.S. Japan treaty rate on interest payments is 10%. To recover the 2016 $20,000 of discovered overwithholding on Customer A, Antelope chooses to apply the set-off procedure to the March 10, 2017 interest payment to Customer A. Instead of 10% or $80,000, Antelope withholds and deposits only $60,000 from the $800,000 interest payment to Customer A. This is equivalent to withholding the correct $80,000 on the 2017 payment and repaying the $20,000 of 2016 overwithholding to Customer A.
▪ When Antelope files its 2016 Forms 1042-S and Form 1042 on March 13, 2017:
  − On #3c the 2016 Form 1042-S to Customer A shows $30,000 of actual 2016 withholding, only 10% liability, $10,000 total withholding credit and $20,000 as amount repaid to recipient.
  − On #3d page 1 of the 2016 Form 1042 shows line 59 liability must be reduced if repaying a BO after year end (before March 15, 2017). But negative liability amounts are not allowed, so Antelope adjusts line 57 instead.
  − On #3e page 2 of the 2016 Form 1042 shows overwithholding of and a carryforward credit of $20,000.
▪ The 2017 Form 1042-S to Customer A shows $800,000 of gross income, 10% tax rate and $80,000 of federal tax withheld. That is, the 2017 Form 1042-S would not show that set-off was used in 2016.
▪ On #3f page 2 of the 2017 Form 1042 shows $20,000 less of deposits than was withheld, which uses up the $20,000 2016 credit.

Adjustments for Overwithholding on Form 1042

Description

#3c Overwithholding Fixed Using Set-off Procedures

Form 1042-S for 2016

Form 1042-S — Foreign Person's U.S. Source Income Subject to Withholding — 2016 — OMB No. 1545-0096 — Copy A for Internal Revenue Service

Field	Value
1 Income code	01
2 Gross income	100,000
3 Chapter indicator. Enter "3" or "4"	3
3a Exemption code	0
4a Exemption code	15
3b Tax rate	.10
7a Federal tax withheld	30,000
10 Total withholding credit	10,000
11 Amount repaid to recipient	20,000
12a Withholding agent's EIN	00-0001234
12b Ch. 3 status code	01
12c Ch. 4 status code	01
12d Withholding agent's name	Antelope Bank
13a Recipient's name	Customer A
13b Recipient's country code	JA
13d City or town, state or province, country, ZIP or foreign postal code	Osaka 536-0087
13e Recipient's U.S. TIN, if any	000-XX-1111
13f Ch. 3 status code	16
13g Ch. 4 status code	23
13j LOB code	01

For Privacy Act and Paperwork Reduction Act Notice, see instructions. — Cat. No. 11386R — Form 1042-S (2016)

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Adjustments for Overwithholding on Form 1042

Description

#3d Overwithholding Fixed Using Set-off Procedures

Form 1042 for 2016 Page 1

Section 1 Record of Federal Tax Liability (Do not show federal tax deposits here)

Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)	Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)	Line No.	Period ending		Tax liability for period (including any taxes assumed on Form(s) 1000)
1	Jan.	7		21	May	7		41	Sept.	7	
2		15		22		15		42		15	
3		22		23		22		43		22	
4		31		24		31		44		30	30,000
5	Jan. total			25	May total			45	Sept. total		30,000
6	Feb.	7		26	June	7		46	Oct.	7	
7		15		27		15		47		15	
8		22		28		22		48		22	
9		29		29		30		49		31	
10	Feb. total			30	June total			50	Oct. total		
11	Mar.	7		31	July	7		51	Nov.	7	
12		15		32		15		52		15	
13		22		33		22		53		22	
14		31		34		31		54		30	
15	Mar. total			35	July total			55	Nov. total		
16	Apr.	7		36	Aug.	7		56	Dec.	7	
17		15		37		15		57		15	280,000
18		22		38		22		58		22	
19		30		39		31		59		31	
20	Apr. total			40	Aug. total			60	Dec. total		280,000

61	No. of Forms 1042-S filed: a On paper		0	b Electronically	2

62 Total gross amounts reported on all Forms 1042-S and 1000:

a	Total U.S. source FDAP income (other than U.S. source substitute payments) reported	62a	1,100,000
b	Total U.S. source substitute payments reported:		
	(1) Total U.S. source substitute dividend payments reported	62b(1)	
	(2) Total U.S. source substitute payments reported other than substitute dividend payments . . .	62b(2)	
c	Total gross amounts reported (Add lines 62a-b)	62c	1,100,000
d	Enter gross amounts actually paid if different from gross amounts reported	62d	

Examples of the Process (cont'd)

Adjustments for Overwithholding on Form 1042
Description

#3e Overwithholding Fixed Using Set-off Procedures

Form 1042 for 2016 Page 2

Form 1042 (2016)   Page **2**

63	Total tax reported as withheld or paid by withholding agent on all Forms 1042-S and 1000:		
a	Tax withheld by withholding agent	63a	330,000
b	Tax withheld by other withholding agents:		
	(1) For payments other than substitute dividends	63b(1)	
	(2) For substitute dividends	63b(2)	
c	Adjustments to withholding:		
	(1) Adjustments to overwithholding	63c(1)	(20,000)
	(2) Adjustments to underwithholding	63c(2)	
d	Tax paid by withholding agent	63d	
e	**Total tax reported as withheld or paid** (Add lines 63a-d)	63e	310,000
64	Total net tax liability		
a	Adjustments to total net tax liability	64a	
b	Total net tax liability under chapter 3	64b	310,000
c	Total net tax liability under chapter 4	64c	
d	Excise tax on specified federal procurement payments (Total payments made x 2%)	64d	
e	**Total net tax liability** (Add lines 64a-d)	64e	310,000
65	Total paid by electronic funds transfer (or with a request for extension of time to file):		
a	Total paid during calendar year	65a	330,000
b	Total paid during subsequent year	65b	
66	Enter overpayment applied as credit from 2015 Form 1042	66	
67	Credit for amounts withheld by other withholding agents:		
a	For payments other than substitute dividend payments	67a	
b	For substitute dividend payments	67b	
68	**Total payments.** Add lines 65 through 67	68	330,000
69	If line 64e is larger than line 68, enter balance due here	69	
70a	Enter overpayment attributable to overwithholding on U.S. source income of foreign persons	70a	20,000
b	Enter overpayment attributable to excise tax on specified federal procurement payments	70b	
71	Apply overpayment (sum of lines 70a and 70b) to **(check one)**:		
	☑ Credit on 2017 Form 1042 or ☐ Refund		

Adjustments for Overwithholding on Form 1042

Description

#3f Overwithholding Fixed Using Set-off Procedures

Form 1042 for 2017 Page 2

Form 1042 (2017)			Page **2**
63	Total tax reported as withheld or paid by withholding agent on all Forms 1042-S and 1000:		
a	Tax withheld by withholding agent	63a	80,000
b	Tax withheld by other withholding agents:		
	(1) For payments other than substitute dividends	63b(1)	
	(2) For substitute dividends	63b(2)	
c	Adjustments to withholding:		
	(1) Adjustments to overwithholding	63c(1)	)
	(2) Adjustments to underwithholding	63c(2)	
d	Tax paid by withholding agent	63d	
e	**Total tax reported as withheld or paid** (Add lines 63a-d)	63e	80,000
64	Total net tax liability		
a	Adjustments to total net tax liability	64a	
b	Total net tax liability under chapter 3	64b	80,000
c	Total net tax liability under chapter 4	64c	
d	Excise tax on specified federal procurement payments (Total payments made x 2%)	64d	
e	**Total net tax liability** (Add lines 64a-d)	64e	80,000
65	Total paid by electronic funds transfer (or with a request for extension of time to file):		
a	Total paid during calendar year	65a	60,000
b	Total paid during subsequent year	65b	
66	Enter overpayment applied as credit from 2016 Form 1042	66	20,000
67	Credit for amounts withheld by other withholding agents:		
a	For payments other than substitute dividend payments	67a	
b	For substitute dividend payments	67b	
68	**Total payments.** Add lines 65 through 67	68	80,000
69	If line 64e is larger than line 68, enter balance due here	69	
70a	Enter overpayment attributable to overwithholding on U.S. source income of foreign persons	70a	
b	Enter overpayment attributable to excise tax on specified federal procurement payments	70b	
71	Apply overpayment (sum of lines 70a and 70b) to (check one): ☐ Credit on 2018 Form 1042 or ☐ Refund		

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Other Considerations / Impact to Audit

Adjustments for Overwithholding on Form 1042	
Considerations	**Resources**
None at this time.	

Index of Referenced Resources

Adjustments for Overwithholding on Form 1042
Pub. 515 - *Withholding of Tax on Nonresident Aliens and Foreign Entities*
Form 1042 - *Annual Withholding Tax Return for U.S. Source Income of Foreign Persons*
Form 1042 Instructions
Form 1042-S - *Foreign Person's U.S. Source Income Subject to Withholding*
Form 1042-S Instructions
Treas. Reg. 1.1461-2 - *Adjustments for Overwithholding or Underwithholding of Tax*
Treas. Reg. 1.1464-1 - *Refunds or Credits*
Treas. Reg. 1.6414-1 - *Credit or Refund of Tax Withheld on Nonresident Aliens and Foreign Corporations*

Training and Additional Resources

Adjustments for Overwithholding on Form 1042	
Type of Resource	**Description(s)**
Other Training Materials	▪ *How to Audit a Claim for Refund or Credit* - 2015 (IBC) CPE

Glossary of Terms and Acronyms

Term/Acronym	Definition
BO	Beneficial Owner
TWC	Total Withholding Credit
WA	Withholding Agent

Index of Related Practice Units

Associated UIL(s)	Related Practice Unit
9424	*FDAP Income*
9424	*FDAP Payments Source of Income*
9424	*FDAP Withholding under Chapter 3*