

Part III - Administrative, Procedural, and Miscellaneous

Withholding on Wages of Nonresident Alien Employees Performing Services Within the United States

Notice 2009-91

I. PURPOSE

This notice modifies the rules in Notice 2005-76, 2005-2 C.B. 947, for determining the amount of income tax employers must withhold under section 3402 of the Internal Revenue Code (Code) from wages paid for services performed by nonresident alien employees within the United States. The modification is effective with respect to wages paid on or after January 1, 2010.

Notice 2005-76 provides rules for determining the amount of withholding on wages paid to nonresident alien employees. These rules need to be modified to reflect changes made in the withholding tables as a result of the enactment of section 36A of the Code (the "Making Work Pay Tax Credit") in the American Recovery and Reinvestment Act of 2009 (Public Law No. 111-5) (ARRA). Nonresident alien individuals are not eligible for the Making Work Pay Tax Credit under section 36A. The modified rules provide for withholding on the wages of nonresident alien employees that more closely approximates their income tax liability.

II. BACKGROUND

A. Income Tax Withholding on Wages of Nonresident Alien Employees

Generally, employers are liable for the withholding of income tax on remuneration for services performed within the United States by a nonresident alien employee. Section 3402(a)(1) of the Code provides that, except as otherwise provided in section 3402, every employer making a payment of wages shall deduct and withhold from such wages a tax determined in accordance with tables or computational procedures prescribed by the Secretary. Section 3402(a)(1) further provides that any tables or procedures prescribed under section 3402(a)(1) shall be in such form, and provide for such amounts to be deducted and withheld, as the Secretary determines to be appropriate to carry out the purposes of chapter 1 (imposition of individual income tax).

Income tax withholding tables in Publication 15 (Circular E), Employer's Tax Guide, for use with the percentage and wage bracket methods of withholding, are based on the assumption that the employee receiving the wages is entitled to a standard deduction in determining his or her income tax liability. However, in the case of a nonresident alien individual, section 63(c)(6)(B) provides that the standard deduction shall be zero. Notice 2005-76 addresses this difference in treatment by directing an employer to add an amount to the wages of a nonresident alien employee solely for purposes of calculating the income tax withholding for each payroll period.

B. Making Work Pay Tax Credit

Section 36A, which was added to the Code by the ARRA, provides a credit against income tax to an eligible individual in an amount equal to the lesser of (1) 6.2 percent of earned income, or (2) \$400 (\$800 in the case of a joint return). The credit is

reduced or completely eliminated for individuals with modified adjusted gross income exceeding threshold amounts. Section 36A(d)(1)(A)(i) provides that an eligible individual for purposes of section 36A does not include a nonresident alien individual. As currently enacted, the Making Work Pay Tax Credit does not apply to taxable years beginning after December 31, 2010. See section 36A(e). Under the ARRA, taxpayers' reduced tax liability under the provision is expeditiously implemented through revised income tax withholding. See H.R. Conf. Rep. 111-16, 111th Cong., 1st Sess. (2009) at 517. Accordingly, the income tax withholding tables have been revised to take the Making Work Pay Tax Credit into account in determining the amount of income tax to be withheld.

C. Reason for Change to Withholding Procedures for Nonresident Alien Employees

The income tax withholding tables reflect two tax benefits for which nonresident alien employees are not eligible: (1) the standard deduction; and (2) the Making Work Pay Tax Credit. If adjustments from the generally applicable procedures for using the income tax withholding tables are not made in determining income tax withholding for nonresident alien employees, the withholding on the wages of such employees will generally be less than their tax liability. This notice modifies the rules for employers to use in calculating income tax withholding on nonresident alien employees to offset the effects of both the standard deduction and Making Work Pay Tax Credit as assumed under the withholding tables.

The modification applies only to the procedure used by employers in calculating income tax withholding on wages paid to nonresident alien employees as set forth in

part III.B. of Notice 2005-76. The requirements in Notice 2005-76 (part III.A.) relating to the completion of Form W-4, Employee's Withholding Allowance Certificate, by nonresident alien employees, continue in effect.

III. WITHHOLDING RULES THAT WILL BE IN EFFECT FOR NONRESIDENT ALIEN EMPLOYEES ON OR AFTER JANUARY 1, 2010

Beginning with wages paid on or after January 1, 2010, employers are required to calculate income tax withholding under section 3402 of the Code on wages of nonresident alien employees by making two modifications rather than the one modification described in Notice 2005-76 (part III.B). First, employers need to add an amount to wages before determining withholding under the wage bracket or percentage method in order to offset the standard deduction built into the withholding tables. Second, employers need to determine an additional amount of withholding from a separate table applicable only to nonresident alien employees to offset the effect of the Making Work Pay Tax Credit built into the withholding tables. The specific steps to be followed for each of these two modifications will be set forth in Publication 15 and other IRS forms or publications.

IV. EFFECT ON OTHER DOCUMENTS

Notice 2005-76 is modified for wages paid after December 31, 2009, during any period when the Making Work Pay Tax Credit provided under section 36A is in effect.

V. DRAFTING INFORMATION

The principal author of this notice is Alfred G. Kelley of the Office of Associate Chief Counsel (Tax Exempt & Government Entities). For further information regarding this notice contact Alfred G. Kelley on (202) 622-6040 (not a toll-free call).