



## Goldstein & Guilliams PLC

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### **TAX WITHHOLDING REQUIREMENTS FOR FOREIGN GUEST ARTISTS**

As a general rule, any U.S. individual or entity (such as a performing arts organization) that pays money to a foreign artist or foreign artist group, directly or indirectly, is required to withhold 30% of the artist's GROSS compensation.

- The withheld amount is **NOT TAX**. The U.S. does not necessarily keep 30% of the artist's fee. Rather, the withheld amount is submitted to the U.S. government (specifically, the Department of the Treasury) and credited toward the nonresident's actual tax liability.
- When an Artist is subject to withholding, the artist then files a U.S. tax return, in which the artist is able to claim his or her actual expenses and deductions and calculate the actual tax liability. The Internal Revenue Service will then deduct the taxes owed from the withholding, and issue the artist a refund of for the remainder.

#### **Calculating Withholding**

The "gross" includes the artist's fee, as well as any cash reimbursement of expenses. There is a narrow exception for expense reimbursements that meet the three requirements of the IRS's "accountable plan" rules. These requirements are:

1. The expenses must be reasonable and must be directly related to the engagement;
2. The expenses must be substantiated by the artist (i.e., artist must provide receipts); and
3. The expense reimbursement must not be more than the amount of the documented expenses.

If an expense reimbursement meets these three requirements, the reimbursement should not be included in gross compensation for withholding purposes. Expenses that are generally accepted by the IRS to qualify for this type of reimbursement are hotel, travel and meal expenses.<sup>1</sup> Any other expenses, including the amount of any commission paid to a U.S. manager or agent, CANNOT be deducted from the gross.

- If a presenter pays the compensation directly to the foreign artist (or to the artist's foreign manager or agent), then the presenter is responsible for withholding.
- If a presenter pays the compensation to a U.S.-based manager or agent, on behalf of the foreign artist or group, then either the U.S.-based manager/agent OR the presenter may withhold. NOTE – if withholding is required, and neither the manager/agent nor the presenter withholds, then the artist, the manager/agent AND the presenter will all be liable for any tax liability of the foreign artist (although the tax may be collected only once.)

For many years, the IRS did not enforce either the withholding responsibilities of presenters, venues, managers, and agents or the tax liabilities of foreign artists. In other words, everyone just ignored U.S. tax law. As a result, many foreign artists became accustomed to paying NO U.S. taxes and most presenters, venues, managers and agents become accustomed to withholding NO taxes on behalf of foreign artists.

However, several years ago the IRS announced a new enforcement program whereby U.S. presenters, venues, managers and agents would be held liable for foreign taxes not withheld or paid. This is not a change in U.S. tax law, but, rather, an effort to enforce laws that had always been there. It is for this reason that so many presenters, venues, managers, and agents are beginning to insist on either withholding taxes or making sure that the foreign artist or group qualifies for an exemption.

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<sup>1</sup> Note that a cash per diem – where the artist does not provide receipts for the full amount of the per diem – does not qualify for exclusion from gross compensation under these rules.

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The penalty for failure to file a tax return is based in part on the amount of tax owed. So, if no tax is owed, the penalty will be minimal, if there is any at all. Obviously, the IRS's primary concern is the payment of the tax, so, if tax was withheld by the presenter, venue, manager or agent, this will not be an issue. However, there is talk of a future immigration program where anyone applying for a visa to perform in the U.S. will be required to file all delinquent returns before a visa will be issued. Failure to pay taxes or file returns could render an artist, or even an entire group, ineligible to obtain a U.S. visa. This could be a nightmare for some artists who have never filed a tax return and yet have been working in the U.S. for many years. Furthermore, failure to file a timely return results in the artist losing any deductions or exemptions to which he or she may be entitled.

### **Exemptions from Taxation and Withholding**

There are several exemptions from the requirement that 30% of a foreign artist's gross income be withheld:

#### **1. Exemptions Based on Tax Treaties**

The U.S. has entered into tax treaties with approximately 66 countries worldwide which provide for certain exemptions from taxation and/or withholding. There are several types of exemptions in the treaties that would apply to performers.

- Most (but not all) treaties include a limited exemption that applies to individual performing artists
- Most (but not all) treaties include a "business profits" provision that exempts compensation paid to certain foreign businesses (in certain cases, this may include a foreign artist who is an individual independent contractor) from U.S. tax and withholding

Note that every treaty is a bit different from the others, and the treaties themselves are sometimes modified or updated from time to time. In each situation involving a foreign artist, it is prudent to check the IRS website for the latest information on the treaty that is applicable to a particular artist. Each treaty, along with technical explanations and any protocols modifying the treaty are available for viewing and download at <http://www.irs.gov/businesses/international/article/0,,id=96739,00.html>.

#### **a. Distinguishing "Individuals" from "Businesses"**

Before examining the specific exemptions, it is important to determine first if an artist or group of artists is treated as an *individual or individuals* for tax purposes, or if they are treated as a *business*. Merely because a foreign group has incorporated in some way, whether it be here in the U.S. or elsewhere, does not grant "business" status to the group in the eyes of the IRS. The key in making the determination is whether or not the performers in a group "participate in the profits" of the U.S. performances. For instance, let's say that a French musical ensemble with three musicians incorporates itself in France. Payments for the ensemble's services in the U.S. are made payable to the French corporation, and the corporation pays all of the tour expenses for the ensemble. After expenses, the performers split whatever profit (or loss) is left over. Here, the performers are "participating in the profits" and are treated as individuals, not a business, for tax purposes. On the other hand, if the performers receive a set fee or salary from the French corporation for the performances, and this fee or salary is not affected by any profits or loss of the U.S. performances, the performers are not "participating in the profits," and the musical ensemble is treated as a "business" for tax purposes.

Obviously, many cases are clear cut. If one solo artist is performing, and the contract for the performance covers only that artist, the artist is considered an individual (regardless of whether or not the artist has set up a corporation.) On the other hand, when the London Symphony Presenter performs in the U.S., they are treated as a business because the musicians receive a salary and do not "participate in the profits." However, many groups consist of a smaller number of performers, and require a more detailed analysis.

#### **b. Exemptions for Individuals**

An individual foreign artist may be exempt from withholding and/or taxes based on one of a number of different articles that may appear in the treaties:

- The "Artists" article (sometimes called "Artists & Athletes" or "Entertainers") applies to *individual* performing artists and exempts from U.S. taxation compensation paid to foreign artists under certain circumstances.
  - In some instances, if an individual artist is from a specific country, all of the artist's earnings in the U.S. may be tax-free and, thus, not subject to either withholding or taxes. However, this list of countries is quite small, and changes occasionally.
  - In most cases, however, the treaty puts a cap on the amount an individual artist may earn tax-free each year in the U.S. For example, the U.S./U.K. tax treaty permits an artist who is a resident of the U.K. to earn up to 20,000 USD each calendar year before U.S. tax liability applies. However, if an artist earns more than 20,000 USD in that year, the ENTIRE amount earned is subject to U.S. tax. This presents a conundrum for a presenter who is paying a U.K. artist: even if the artist's compensation for

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that presenter's engagement is less than 20,000 USD and, thus, would not be subject to withholding (because there is no tax liability), the presenter has no way of knowing if the artist will earn more than 20,000 USD within the tax year. For this reason, it is usually advisable for the presenter to withhold— even if the artist's compensation is well under the cap. The onus is then on the artist to file a U.S. tax return, claim any applicable exemptions or deductions, and obtain a refund of any amount withheld in excess of the tax owed.

- If there is a tax treaty, but the treaty does NOT include an article that applies specifically to performing artists, then there are several articles that may apply:
  - Many treaties include articles on “Independent Personal Services” or “Dependent Personal Services” that will apply to foreign artists. Generally, the “*Independent Personal Services*” article applies to artists who are independent contractors, while the “*Dependent Personal Services*” article applies to artists who are working as employees of someone else (e.g., the presenter would be hiring someone else to provide the services of the artist.) In these articles, income paid to a performing artist performing services in the U.S. as an *independent contractor* is generally not taxable in the U.S. if the artist has no “fixed base” in the U.S. – e.g., a residence or office. Income paid to a performing artist performing services in the U.S. as an *employee* is generally not taxable in the U.S. if the artist's presence in the U.S. is limited, and the employee is being paid by a non-U.S. entity.
  - The more recent treaties have done away with the “Independent Personal Services” and “Dependent Personal Services” articles, and instead include an “Income from Employment” article. Note, however, that this article applies only to performers who are working as *employees*. In these treaties, the definitions of “business” and “enterprise” now include independent contractors who perform services in the U.S. Accordingly, foreign artists performing as independent contractors may be exempt from taxation under the “Business Profits” article of these treaties.

### c. Exemptions for Businesses

If a group qualifies as a “business” for tax purposes, any compensation paid to the foreign business will likely be exempt from taxation and withholding under the “business profits” article of the applicable tax treaty, provided that the business has no “permanent establishment” in the U.S. (e.g., an office.) However, the individual artists employed by the “business” may be subject to U.S. taxes and be required to file U.S. tax returns.

## 2. Exemptions Based on Tax-Exempt Status

Another exemption that is unrelated to tax treaties is commonly known as the “non-profit” exemption, but this, too, is quite limited. The exemption is available to organizations who have obtained tax-exempt status in their home country and who satisfy one of the following requirements:

- The group must apply for and receive from the IRS a determination letter that their organization would qualify as a tax-exempt entity under § 501(c)(3) of the U.S. tax code. The fact that the organization is considered a tax exempt entity in a foreign country is irrelevant unless the same organization could qualify for tax-exempt status under U.S. law; **OR**
- The organization may obtain a letter from a U.S. attorney certifying that the group WOULD qualify for 501(c)(3) status under U.S. law if they applied.

While most organizations would not qualify for this exemption, the good news (for the organization) is that a foreign tax-exempt organization would qualify for a tax treaty “business profits” exemption from taxation, thus avoiding having to seek an IRS or attorney determination letter. However, a “determination letter” could be the only option for an organization from a country with whom the U.S. does NOT have a tax treaty. The organization either could apply to the IRS for a determination letter or pay an attorney for the same determination. If the organization performs frequently in the U.S., this may be a cost-effective measure to avoid both withholding and taxation. However, once again, the individual artists employed by the “business” may be subject to U.S. taxes and be required to file U.S. tax returns.

## 3. Exemption Based on Central Withholding Agreement

A Central Withholding Agreement (CWA) is a contract entered into between the IRS, the foreign artist, and a designated “withholding agent.” The withholding agent may be the artist's agent or manager, a presenter (including a presenter), an accountant, or anyone else who is acceptable both to the artist and the IRS. If the artist obtains a CWA, the IRS will estimate the *actual* tax that the artist will owe, and this amount will be withheld from the artist's income. As noted above, because an artist who is an independent contractor may deduct certain business expenses from his or her taxable income, and because the artist will be taxed at graduated rates (which are often less than 30%), the amount withheld pursuant to a CWA will likely be reduced substantially from the standard 30% withholding rate.

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Note that CWAs are available ONLY to individuals, not to businesses. Artists should submit their request for a CWA to the IRS no later than 45 days prior to their first U.S. engagement.

If a foreign artist enters into a CWA, the artist must furnish a copy of the CWA to anyone paying for his or her services – e.g., a U.S. presenter. The presenter must then withhold only the amount designated by the CWA – not 30% of the artist's gross income – and submit the amount withheld to the designated “withholding agent.” The withholding agent is then responsible for submitting the withheld taxes to the IRS.

### **How the Foreign Artist Claims an Exemption**

To claim an exemption, the procedure depends on which exemption is being claimed:

- If an individual is claiming a tax treaty exemption, he or she must complete Parts I, II and III of IRS Form 8233 and submit it to the presenter.
  - If the individual is from a country where there is no cap on the amount an individual artist may earn tax-free in the U.S. and all of the artist's income is tax-free, then the presenter reviews the form for accuracy, completes Part IV of the form, and **forwards the form, along with any attachments, to the IRS** within five days of receipt. Note that the presenter should file Form 8233 with the IRS **prior to making the first payment**. The exemption from withholding is effective for payments made beginning ten days *after* the form is *mailed* to the IRS. (Remember that any in-kind payments or third-party payments such as airfare, hotel accommodations, and other costs are also considered compensation paid to the foreign independent contractor artist.) Form 8233 is valid only for the calendar year in which it is filed and must be refiled each year.
  - On the other hand, if the individual is from a country where there is a cap on the amount an individual artist may earn tax-free in the U.S., then the presenter has no way of knowing if the artist will earn more than 20,000 USD within the tax year. In this instance, the artist will be subject to withholding. At the end of the tax year, if the artist has earned less than the cap, the artist will file a U.S. tax return and attach Form 8233 to claim his or her exemption. The artist will then be entitled to a refund of the full amount of the withholding.
- If a business is claiming an exemption under the “business profits” treaty article, the business must complete IRS Form W-8BEN and provide it to the presenter. Unlike Form 8233, Form W-8BEN is not submitted to the IRS. The form is retained by the presenter, and is presented to the IRS only in the event that the IRS questions why taxes were not withheld by the presenter at the time of payment.
- If a group is claiming a “tax-exempt” exemption, the business must complete IRS Form W-8EXP and provide it to the presenter, along with an IRS determination letter or an opinion letter of U.S. counsel that the group qualifies for 501(c)(3) status. Unlike Form 8233, Form W-8EXP is not submitted to the IRS. The form is retained by the presenter, and is presented to the IRS only in the event that the IRS questions why taxes were not withheld by the presenter at the time of payment.

One important note regarding the above-referenced forms – none of them is valid for the purpose of claiming an exemption without a taxpayer identification number (TIN) or a Social Security Number (SSN), whichever is applicable.

### **Obtaining TINs and SSNs**

- For businesses, the TIN must be an IRS-issued Employer Identification Number (EIN).
- For individuals, the TIN will be either a Social Security Number (SSN) or an IRS-issued Individual Tax Identification Number (ITIN). While an EIN is relatively simple to obtain, the same cannot be said of a SSN or ITIN:
  - An artist cannot apply for an ITIN without first attempting to obtain an SSN. To obtain a SSN, an individual must apply in person at a Social Security office here in the U.S. Any artist in the U.S. on an “O” or “P” visa is entitled to receive a SSN. When the artist enters the country, he or she will receive an “I-94” card, which includes certain information related to the individual's visa and work-authorization status. After the individual enters the U.S., the I-94 information is eventually entered into a government computer. This can take up to ten days. For this reason, the Social Security Administration requests that a foreign artist wait at least ten days after entering the U.S. before applying for the SSN. An applicant's request for a SSN will be denied if his or her I-94 information is not accessible to the Social Security Administration. If an artist's application for an SSN is denied for any reason, then the Artist may apply for an ITIN. However, proof of the SSN denial must be provided.

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## Depositing Withheld Taxes

If withholding is required of a presenter (or anyone else in the U.S. making payments for the services of foreign artist), certain procedures must be followed with regard to depositing and remitting the tax withheld to the IRS. Withholding agents are required to pay the tax withheld on an annual, monthly, or quarter-monthly basis, *depending on the amount withheld*. The tax must be deposited with the federal government through the Electronic Federal Tax Payment System (“EFTPS”).<sup>2</sup>

A quarter-monthly period means one of the following: (1) the first day of the month through the seventh day; (2) the eighth through the fifteenth; (3) the sixteenth through the twenty-second; or (4) the twenty-third through the end of the month. If at the end of any quarter-monthly period, the total amount of *accumulated* undeposited tax is greater than \$2,000, such tax must be paid within three (3) business days of the end of such quarter-monthly period. The quarter-monthly deposit requirement will be considered as having been satisfied if the withholding agent deposits 90 percent of the tax withheld during the period within three banking days after the close of the period. The remainder of the deposit must be made with the first deposit required after the fifteenth day of the following month.

Monthly deposits are required if, at the end of any month, the total amount of accumulated undeposited tax is more than \$200 but less than \$2,000. The aggregate amount of withheld tax is required to be deposited within fifteen days after the close of the calendar month.

Annual deposits are required if at the close of the calendar year the total amount of accumulated undeposited tax is less than \$200. The deposit of such amount may be remitted with Form 1042 or by the due date for the Form 1042.

## Withholding Agent Tax Forms

### 1. **Form 1042 – Annual Withholding Tax Return for U.S. Source Income of Foreign Persons**

This return must be completed by anyone making a payment for the services of a foreign artist (e.g., a U.S. presenter.) **Form 1042 must be filed regardless of whether any tax was withheld on payments to foreign artists.** This form is a tax return filed by a withholding agent to summarize the total amount of income paid to foreign artists, as well as all tax withheld, in the aggregate. Forms 1042-S and if appropriate, Form 8233 (required for tax treaty exemptions for individuals) must accompany Form 1042 when it is filed with the IRS. Form 1042 should be filed by March 15 of the year following the calendar year in which the payments were made.

### 2. **Form 1042-S – Foreign Person’s U.S. Source Income Subject to Withholding**

Form 1042-S is issued to a foreign artist by a U.S. presenter making a payment for the services of that foreign artist. This form is similar in purpose to Forms W-2 and 1099 and serves to replace such forms for the reporting of most income paid to foreign artists (i.e., if the foreign artist is an independent contractor, the income paid to the performer should be reported on Form 1042-S.) A separate Form 1042-S must be filed for each foreign artist to whom or on behalf of whom a presenter makes payments. A foreign artist’s taxpayer identification number is required on Form 1042-S if the artist either seeks credit for the taxes withheld or a tax treaty tax exemption. By March 15 of the year following the calendar year in which the payments were made, the presenter must give the foreign artist copies B through D of Form 1042-S, and file Copy A with Form 1042.

## STATE TAXES

The above comments address only U.S. federal tax law—that is, taxes imposed by the federal government. However, each of the 50 states may impose their own tax withholding and payment obligations on foreign artists performing in their states. Few states are enforcing this. However, this, too could change, so it is always an issue to be aware of.

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<sup>2</sup> While payments used to be accepted by a federal reserve bank and certain commercial banks with a Federal Tax Deposit Form 8109, this system is being phased out of use. The IRS currently requests that all deposits be made online through EFTPS.

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## **RESOURCES FOR ADDITIONAL INFORMATION**

1. [www.artistsfromabroad.org](http://www.artistsfromabroad.org). This website is a valuable resource for those engaging foreign artists to perform in the U.S. The site includes information on obtaining visas for foreign artists to enter the U.S. and on taxation and withholding with regard to foreign artists.
2. [www.irs.gov](http://www.irs.gov). The website of the Internal Revenue Service is a valuable source of information that includes complete tax treaties with explanations, forms and publications that offer guidance as to both withholding and taxation. Publications relevant to taxation of foreign guest artists are Publication 515 ("Withholding of Tax on Nonresident Aliens and Foreign Entities"); Publication 519 ("U.S. Tax Guide for Aliens") and Publication 901 ("U.S. Tax Treaties").
3. Our law firm is nationally and internationally known in the field of performing arts law and, in particular, with regard to issues affecting foreign artists wishing to perform in the U.S. We will be happy to provide individual consultations on this or any other arts-related legal topic.

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