

Notice 2015-10: IRS intends to amend regulations for refund and credit claims for Chapters 3 and 4 overwithholding

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Future IRS Regulations Intend to Limit Chapter 3 and 4 Overwithholding Refund and Credit Claims to the Amount Deposited by Withholding Agent

On April 28, 2015, the Internal Revenue Service (“IRS”) released **Notice 2015-10: Guidance on Refunds and Credits under Chapter 3, Chapter 4, and Related Withholding Provisions**. In the Notice, the IRS announced its intent to amend the U.S. Treasury Regulations applicable to claims for refund or credit for amounts overwithheld under Chapters 3 and 4.

As a response to IRS concerns about refunds and credits issued to non-resident aliens before the full amount of tax had been collected, the amended regulations would aim to prevent claimants from obtaining a refund or credit that is in excess of the amount that has been deposited by the withholding agent. This change will limit refund and credit claims, even when the claimant can demonstrate that the amount of withholding reported by the withholding agent on Form 1042-S was in excess of the amount required under Chapter 3 or 4.

The amended regulations will apply to refund and credit claims for amounts withheld with respect to calendar year 2015 and later.

Refund and Credit Claims under the Amended Regulations

Notice 2015-10 indicates that the amended regulations will provide a general rule, as well as a pro rata allocation for refund and credit claims where the withholding agent has made a partial deposit.

General Rule

Under the amended regulations, the IRS will restrict claimants from receiving refunds or credits for amounts withheld under Chapter 3 or 4 when there is a shortfall in the deposits required to be made by the withholding agent for the calendar year. If the withholding agent has not deposited any withholding for the particular calendar year, then the IRS will not permit any refund or credit claims for claimants whose payments were overwithheld by the withholding agent.

Allocation of Partial Deposits to Refund or Credit Claims

While the IRS intends to restrict claimants' refund and credit claims when the withholding agent has failed to deposit the full amount of withholding required to be reported on its annual Form 1042, the IRS recognizes that a withholding agent may have deposited a portion of the amount withheld under Chapter 3 or 4. When the withholding agent has made a partial deposit to the IRS, the claimant will be entitled to claim a partial refund or credit.

The IRS determines the amount of the partial refund or credit to any particular claimant by prorating the deposits made by the withholding agent. For example, if a withholding agent has deposited 75% of the total tax amount due to the IRS at the time of the claim, then the IRS will permit a refund or credit claim for 75% of the amount of withholding reported on the claimant's Form 1042-S, reduced by the appropriate amount of withholding. Therefore, if a withholding agent withheld \$30 instead of \$10, then the claimant will be entitled to a partial refund or credit of \$12.50 ($\$30 \times 75\% - \10).

Exceptions

The IRS is considering exceptions to the general and partial allocation rules that would be administrable by the IRS but also minimize the potential for fraud or intentional under-deposit of withholding taxes. As examples, the IRS is contemplating whether to provide an exception if the under-deposit is de minimus or the withholding agent has a demonstrated history of compliance with the deposit rules.

IRS Request for Comments

The Notice requests public comments regarding the allocation of partial deposits and procedural rules, as well as the potential exceptions the rules in the Notice (both noted and any others consistent with purpose of the Notice). Comments must be submitted to the IRS either by mail or electronically via the [Federal eRulemaking Portal](#) by June 29, 2015.

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