



IRS Clarifies Requirements for ITINs (Form W-7) Related to Royalty Income

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A FEW YEARS AGO the Internal Revenue Service issued regulations that increased the compliance burden related to the reporting and withholding requirements on payments to foreign persons. When these rules became effective, Marcum & Kliegman LLP reported to the literary community the various details of those compliance issues. By now, we all understand that without the required documentation, the withholding agent (generally the publisher or the literary agency) is required to withhold U.S. taxes at a 30% rate on the foreign person's share of income. As the penalties for failing to comply with the rules are substantial, most literary agencies quickly adopted procedures to assist their foreign clients in the process of completing the Forms W8-BEN and related W-7. In December 2003, the IRS announced changes in the application process to "help ensure that Individual Tax Identification Numbers ("ITINs") are issued for their intended tax purpose." In other words, due to homeland security issues, the IRS now requires additional information and documentation to be submitted with the Form W-7.

WHAT ARE THE NEW REQUIREMENTS?

At first glance, these new requirements seemed onerous. In order for the IRS to confirm the appropriateness of a foreign authors application, the foreign author would need to attach their original U.S. Income Tax Return. If the author was not required to file a U.S. tax return, then they would need to show they have an asset that generates income subject to reporting requirements. What does this mean? Perhaps this would mean a copy of part of the publishing contract would need to be submitted with the Form W-7. Naturally, this interpretation, if correct, would be of great concern to authors, agents and publishers. In swift response

to this concern, a coordinated written request for clarification was sent to the IRS on behalf of the Association of Authors' Representatives (AAR), the Authors' Guild, and the Association of American Publishers (AAP).

CLARIFICATION FROM THE IRS

In April, the Director of the ITIN Program promptly responded with a practical resolution to this matter. The Director advises that income from Royalties (which, of course, includes advances) is "passive income" and falls under an exception to the documentation requirements.

The Director also provides us specific instructions to assist in the completion of the Form W-7 as follows:

- The applicant should check box "h" ("Other") and enter in the space to the right, "Royalties."
- If the author is entitled to a reduced rate of tax due to a tax treaty, then box "a" should be checked and the name of the tax treaty country and tax treaty article number must be provided.
- Documentation is needed regarding royalty income. This is needed to satisfy the requirement that the author "shows they have an asset that generates income subject to reporting requirements." The documentation can be a letter from the

author's publisher written to the author indicating the existence of the contractual relationship. This letter would also need to include the publisher's Employer Identification Number, the author's name and foreign address. Of course, all of the previous requirements, such as the mandatory form of identification remain the same.

This is merely an overview of the latest changes to a very complicated set of regulations. There are specific aspects of these rules that may have an effect upon your particular circumstances. Failure to comply with the new requirements will result in the rejection of the application and a delay in the ability to make payments to foreign persons. Therefore, whether you are an agent, author or publisher, it is important to consult your tax advisor to be sure you comply with these rules. 

