

Policy on Tax Treatment of Payments Made to Individuals

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Effective Date: October 1, 2013

Reason for Policy

Last Updated: June 23, 2016

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POLICY STATEMENT

It is the policy of the University to comply with the income and employment tax withholding and reporting requirements established by the Internal Revenue Service (IRS), the California Franchise Tax Board (FTB), and local tax authorities. The University also complies with the withholding and reporting requirements established by other states and localities in connection with employees who are hired or assigned to work outside of California.

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REASON FOR POLICY

This Policy summarizes the tax withholding and reporting requirements for payments made through the University's accounts payable (AP), payroll, and student systems to, or on behalf of, individuals who are U.S citizens or resident aliens. Further information is provided in the

applicable policy covering each payment type. See **Related Information**. For information regarding payments made to foreign individuals, see **Nonresident Aliens Payments Policy**.

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WHO SHOULD READ THIS POLICY

Any employee who is responsible for approving payments to individuals on behalf of the University; the members of the Leadership Team, as well as supervisors and Business Managers who supervise an employee with such responsibilities.

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POLICY TEXT

This Policy provides general information on the federal and state tax reporting and withholding requirements governing payments made to U.S. citizens and resident aliens through the University's payroll and AP systems. The Policy also covers scholarship and fellowship payments made to students through the student system. Regardless of the payment system, all amounts disbursed by the University are subject to withholding and reporting in accordance with the requirements established by the IRS, the FTB, and other tax authorities that have jurisdiction over the University. As the withholding agent, the University is responsible for withholding the correct amount of tax associated with its payment activities and promptly depositing those taxes with the appropriate government agencies.

Appendix A includes a table summarizing the income and FICA (i.e., social security and Medicare) tax withholding and reporting requirements associated with numerous types of payments commonly made by the University. Because it would not be possible to include all payments in the table, Business Managers should consult the related University policies referenced below or contact the Office of Accounting and Business Services (ABS) for additional information.

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RELATED INFORMATION

Type	Title
USF	Department Payroll Controls Policy - <i>Under construction</i>
USF	Electronic Communication Policy
USF	Honorarium Payments Policy
USF	Independent Contractor Policy
USF	Membership Policy
USF	Moving Reimbursement Policy
USF	Non-Cash Gifts, Awards and Incentives Policy
USF	Nonresident Alien Payments Policy
USF	Student Employment Policy
USF	Travel and Entertainment Policy
External	IRS Publication 15-B, Employer’s Tax Guide to Fringe Benefits
External	IRS Publication 505, Tax Withholding and Estimated Tax
External	IRS Publication 970, Tax Benefits for Education
External	FTB Publication 1017, Resident and Nonresident Withholding Guidelines

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DEFINITIONS

Term	Definition
Business Manager	A University employee, designated by the President, Vice President, Vice Provost, or Dean who is the financial manager for the University account(s) being used for the expense. This may include the President, Vice Presidents, Vice Provosts, or Deans.
FICA (Federal Insurance Contributions Act)	FICA is a two-part employment tax consisting of social security and Medicare. Half of the payment is made by the employee and the

other half by the University. Employees normally pay 6.2% of their wages for social security, up to the wage limit, and 1.45% of their total covered wages for Medicare. The University also pays 6.2% and 1.45% for social security and Medicare, respectively. An additional .09% in Medicare tax is withheld from an employee's wages in excess of \$200,000. The additional .09%, however, applies only to employees, not the University.

Scholarship or Fellowship An amount paid to, or on behalf of, an individual for the primary purpose of assisting the person in the pursuit of his or her studies or research. Such amounts include grants, waivers, and other forms of gift aid that typically do not have to be repaid by the recipient.

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ADDITIONAL CONTACTS

Subject	Contact	Phone	Email/URL
ABS	Frank Wasilewski	415.422.2402	fmwasilewski@usfca.edu
Tax Compliance	Dominic Daher	415.422.5124	dldaher@usfca.edu
Disbursement Services	Dennis Miller	415.422.2102	millerd@usfca.edu

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FORMS

Form	Use	Location
Out-of-State Income Tax Withholding Form	Used by employees to request withholding in another state.	Human Resources
Form 590	Used to claim exemption from nonresident California withholding.	FTB
Form 592	Used to report the total amount or resident and nonresident California withholding.	FTB

Form 592-B	Used to report to a nonresident payee the amount of California withholding on nonwage payments received by the individual for services performed in California.	FTB
Form 1098-T	Used to report gift aid and expenses to assist taxpayers in claiming educational credits and deductions.	IRS
Form 1099-MISC	Used to report certain income payments of \$600 or more made to non-employees.	IRS
Form W-2	Used to report wage payments made to employees	IRS

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RESPONSIBILITIES

Department/Business Manager

- Responsible for ensuring payments made to its employees, students, and other individuals are made in accordance with this Policy and related University policies.

Accounting and Business Services

- Processes all AP, payroll, and student payments made by the University in accordance with applicable federal, state, and local tax laws and regulations.
- Prepares Forms W-2 and 1099-MISC for distribution to payees and the IRS.
- Reviews any requests for an exception to this Policy in consultation with the Director of Internal Audit and Tax Compliance.

Office of Internal Audit and Tax Compliance

- Prepares Forms 592-B for distribution to California nonresident payees and the FTB.
- Prepares Forms 592 for distribution to the FTB on a quarterly basis.
- Administers the GLACIER Nonresident Alien Tax Compliance System and prepares Forms 1042-S for distribution to payees and the IRS.
- Determines whether an employee working in a state outside of California is subject to income tax withholding in that state.
- Determines whether a worker should be classified as an employee or an independent contractor.

- Reviews any requests for an exception to this Policy in consultation with the Associate Vice President for Accounting and Business Services.

One Stop Enrollment and Financial Services

- Prepares Forms 1098-T for distribution to students and the IRS.

President, Vice Presidents, Vice Provosts, and Deans

- Ensures that departments within his or her division are in compliance with this Policy and related University policies.

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FREQUENTLY ASKED QUESTIONS

(N/A)

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REVISION HISTORY

- 06/23/2016 – Updated to clarify tax treatment of cash prizes and awards paid to students and to include technical changes.
- 03/10/2016 – Revised to provide additional guidance on the withholding of California income tax from nonresidents of the state.
- 05/12/2015 – Updated to include hyperlinks and references to the Independent Contractor Policy, Nonresident Alien Policy, and Student Employment Policy.
- 10/01/2013 – First publication of Policy.

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APPENDICES

Appendix A - Tax Treatment of Payments Made to Individuals

Appendix B - Scholarship and Fellowship Recipients, General Tax Information

PROCEDURES

- **Authorization**
- **AP System Payments**
- **Payroll System Payments**
- **Student System Payments**
- **Payments to Foreign Individuals**
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AUTHORIZATION

Payments made by the University are subject to reporting and withholding as determined by applicable federal and state tax laws and regulations. Departments are not authorized to implement procedures that deviate from those set forth in this Policy. Any exception to this Policy requires approval by both the Associate Vice President for Accounting and Business Services and the Director of Internal Audit and Tax Compliance.

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AP SYSTEM PAYMENTS

This section summarizes the withholding and reporting requirements for payments made to individuals through the AP System.

Payments to Non-Employees

Compensation-related payments made to a non-employee for performing independent personal services are reportable on IRS Form 1099-MISC if the total payments made to the individual are \$600 or more for the calendar year. Such payments include consulting, speaking and performance fees, honoraria, and similar service payments. Payments for non-cash gifts, prizes, and awards presented to a non-employee and payments of other income made to a non-employee of at least \$600 are also reportable on Form 1099-MISC. These payments are not subject to withholding provided that the individual has furnished ABS with a valid taxpayer identification number (TIN), e.g., social security number. If a payee fails to provide his or her TIN, or the TIN provided is incorrect, then the payment will be subject to backup withholding at the rates of 28% (federal) and 7% (California).

Pursuant to California Revenue & Tax Code Section 18662, withholding at a rate of 7% is required on certain payments to nonresidents of California on California source income. This includes payments for non-wage service payments (such as payments to independent contractors), but only if the services are performed within the State of California and exceed

\$1,500 in total for the calendar year in question. The foregoing payments are reported by Internal Audit and Tax Compliance to the California Franchise Tax Board on Forms 592 and 592-B. **Non-wage service payments to service providers who perform services outside of California are not subject to California withholding.**

California withholding is required on applicable payments not only to individuals, but also to business entities (including corporations, partnerships and LLCs) that do not have a permanent place of business in California or that have not registered with the California Secretary of State to do business within the State of California. California Form 590 (Withholding Exemption Certificate) should be collected from any out-of-state service provider performing services within California to determine whether an exemption applies. **See FTB Publication 1017, Resident and Nonresident Withholding Guidelines.**

Payments to Employees

Any taxable payment made to an employee or on behalf of an employee is subject to withholding and reporting as provided below. In general, such payments should be paid through the payroll system rather than the AP system. However, if it would not be possible to make a payment through payroll (e.g., temporary housing, life insurance, etc), the details of the payment must be provided to Payroll Services in a timely manner so that applicable income and employment taxes may be withheld from the employee's regular wages.

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PAYROLL SYSTEM PAYMENTS

All salary and wage payments made to an employee are reportable on IRS Form W-2 and are subject to withholding of applicable income and FICA taxes. Fringe benefits provided to an employee (or a member of the employee's family) are also taxable, unless specifically excluded from an employee's wages under the Internal Revenue Code. Taxable benefits include, but are not limited to, certain travel and moving expense reimbursements, group-term life insurance coverage in excess of \$50,000, tuition remission in excess of \$5,250 for graduate-level courses that are not job-related, etc.

For additional information regarding employee wage and fringe benefit payments, see IRS Publication 15-B, **Employer's Tax Guide to Fringe Benefits.**

Employees Working Out-of-State

The **Out-of-State Income Tax Withholding Form** must be completed whenever an employee is hired or assigned to work in a state other than California. The completed form should be submitted by the employee to the Office of Internal Audit and Tax Compliance at least ten (10)

business days before the out-of-state assignment begins. Based on the information supplied on the form, the Office of Internal Audit and Tax Compliance will determine whether the employee will be subject to withholding in the state where he or she will be working.

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STUDENT SYSTEM PAYMENTS

This section summarizes the withholding and reporting requirements applicable to payments made to students for scholarships, fellowships, and other forms of gift aid. Payments made to or on behalf of a student for such financial assistance, while initiated in the student system, are disbursed through the AP system. All student assistance payments must originate in the student system so that they are correctly reported on IRS Form 1098-T, which is provided to students for purposes of claiming the federal education tax credits and deductions.

Non-Taxable Scholarships and Fellowships

A scholarship or fellowship is not taxable to the extent that the funds provided under the grant are used for “qualified” expenses and there is no expectation that the recipient perform any substantial services (i.e., either past, present, or future services) in return for receiving the grant. The portion of a grant related to the performance of services represents wages, which must be paid to the recipient through the payroll system. See **Student Employment Policy**.

Assuming that a scholarship or fellowship includes no service requirement, any funds used for qualified expenses are not taxable. Qualified expenses include required tuition, fees, books, supplies, equipment, and other mandatory fees for classes or enrollment. The amount used to pay required health insurance premiums in order for a student to be enrolled is also considered a qualified expense and is not taxable.

Taxable Scholarships and Fellows

Any portion of a scholarship or fellowship used to pay for “nonqualified” expenses such as room and board, travel, moving, and other living expenses is taxable to the recipient. This would be the case regardless of how the funds were paid, i.e., directly to the student or on his or her behalf. See IRS Publication 970, **Tax Benefits for Education**.

The taxable portion of a non-service scholarship or fellowship provided to a U.S. citizen or resident alien is not subject to withholding. The IRS recommends, however, that colleges and universities inform students in writing if part of their scholarship or fellowship is taxable. **Appendix B** includes a summary of the general tax rules governing scholarship and fellowship grants, including the Form 1098-T reporting requirements, which may be provided to students.

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PAYMENTS TO FOREIGN INDIVIDUALS

The University uses the GLACIER Nonresident Alien Tax Compliance System to determine the federal tax treatment of payments made to its foreign students, employees, and other visitors who are temporarily in the United States to work or study on campus. Income paid to a nonresident alien and the withholding on such income is reportable on IRS Form 1042-S. For additional information, see **Nonresident Alien Payments Policy**.

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VIOLATIONS

A violation of any portion of this Policy may result in disciplinary action, up to and including termination of employment and/or legal action.

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Policy on Tax Treatment of Payments Made to Individuals

Appendix A

ACCOUNTS PAYABLE¹

Payment Type ²	Income Taxable?	Wages (withhold income and FICA taxes)?	Reporting Requirement? ³
Cell phone and tablet computer reimbursements ⁴	No	No	None
Honorarium payments ⁵	Yes	No	1099-MISC, Box 7, Nonemployee compensation
Human subject payments	Yes	No	1099-MISC, Box 3, Other income
Independent contractor payments ⁶	Yes	No	1099-MISC, Box 7, Nonemployee compensation
Life insurance coverage over \$50,000	Yes	Yes	W-2
Memberships ⁷	No	No	None. The value of a social membership not used for business purposes, however, is taxed as additional wages.
Moving reimbursements - removal of household effects, transportation, lodging, etc. ⁸	No	Yes	None
Moving reimbursements - meals, temporary housing, house hunting, etc.	Yes	Yes	W-2
Non-cash gifts and awards ⁹	No	No	None
Prizes and awards - cash	Yes	No	1099-MISC, Box 3, Other income
Travel reimbursements ¹⁰	No	No	None
Travel reimbursements - employee trips of more than 1 year	Yes	Yes	W-2
Travel reimbursements - pre-employment interview	No	No	None
Travel advances - excess amount unrecovered	Yes	Yes	W-2
Travel allotments - NCAA	No	No	None

PAYROLL¹¹

Payment Type ²	Income Taxable?	Wages (withhold income and FICA taxes)?	Reporting Requirement? ³
Wages, including overload, overtime, stipend, honorarium, and other pay	Yes	Yes	W-2
Faculty rental subsidy	Yes	Yes	W-2
Merit, bonus, recognition, and similar cash awards	Yes	Yes	W-2
Sabbatical pay	Yes	Yes	W-2
Severance pay	Yes	Yes	W-2
Uniform allowance and similar allowances (e.g., car allowance)	Yes	Yes	W-2
Vacation (including final vacation pay), sick leave, and holiday pay	Yes	Yes	W-2

STUDENT SYSTEM

Payment Type ²	Income Taxable?	Wages (withhold income and FICA taxes)?	Reporting Requirement? ³
Scholarships and Fellowships			
Tuition, fees, books, and required expenses ¹²	No	No	1098-T, Box 2, Amounts billed for qualified tuition and related expenses
Expenses in excess of required expenses (e.g., room, board, travel, stipends, etc.)	Yes	No	Payments for such expenses are not reportable on the 1099-MISC but must be included in Box 5, Scholarships or grants, on the 1098-T. See Appendix B.
Scholarship or fellowship requiring the performance of services ¹³	Yes	Yes	The service portion of the award must be paid through payroll and reported on the W-2.
Prizes and awards – cash (paid through the student system for educational expenses) ¹³	No	No	
Prizes and awards – cash (not paid through the student system)	Yes	No	1099-MISC, Box 3; report on W-2 if student is also an employee.

Employee Tuition Remission¹⁴

Undergraduate courses	No	No	None
Graduate courses, job-related	No	No	None
Graduate courses provided to graduate teaching and research assistants	No	No	None
Graduate courses, not job-related, up to \$5,250 per year	No	No	None
Graduate courses, not job-related, exceeding \$5,250 per year	Yes	No	W-2

1 Taxable payments made to a non-employee totaling \$600 or more for the calendar year are reportable on Form 1099-MISC. Non-wage service payments made to nonresidents of California for services performed within the state are reportable on FTB Form 592-B and are subject to withholding of 7% if the total payments made to the individual are more than \$1,500 for the calendar year. Any taxable payment made to an employee through AP would be reported on the employee's Form W-2, subject to withholding of applicable income and FICA taxes.

2 Payments made to nonresident aliens are subject to separate federal income tax withholding and reporting rules. See **Nonresident Alien Payments Policy.**

3 Under the combined federal and state electronic filing program, the IRS forwards Form 1099-MISC information filed with it to the participating states, including California.

4 See **Electronic Communication Policy.**

5 See **Honorarium Payments Policy.**

6 See **Independent Contractor Policy.**

7 See **Membership Policy.**

8 See **Moving Reimbursement Policy.**

9 See **Non-Cash Gifts, Awards and Incentives Policy.**

10 See **Travel and Entertainment Policy.**

11 Wages paid to an employee who is hired or assigned to work out-of-state may be subject to withholding in that state.

See **Out-of-State Income Tax Withholding Form and instructions.**

12 Payments for both graduate and undergraduate courses are tax-free, including courses taken in a prior academic term or calendar year.

13 See **Student Employment Policy.**

14 For the tax treatment of tuition remission provided to a spouse, domestic partner, or other dependent, see the

Application for Tuition Remission.

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Tax Treatment of Payments Made to Individuals

Appendix B

Scholarship and Fellowship Recipients General Tax Information

The following information is intended for University of San Francisco students (U.S. citizens and residents) who are recipients of a scholarship or fellowship grant. This information includes the general tax rules published by the Internal Revenue Service (IRS) regarding such grants and applies regardless of whether your award is funded by the University or by another source.

The University does not provide tax advice; for additional information, please contact your personal tax advisor or consult the IRS publications referenced below.

Under IRS regulations, the term “scholarship or fellowship” includes grants, waivers, and other forms of gift aid, which typically do not need to be repaid by the recipient of the aid. In some cases, the scholarship or fellowship funds are paid directly to you, while in other cases they are credited to your University student account. Whether the scholarship or fellowship payment is paid to you directly or to the University on your behalf, for tax purposes, the payment is treated as made to you and is subject to the tax rules discussed below.

Is my scholarship or fellowship taxable? You do not have to pay taxes on a scholarship or fellowship to the extent the funds are used for required tuition, fees, books, supplies, equipment, or other mandatory fees for classes or enrollment. The amount of health insurance premiums you pay to the University in order to be enrolled is also considered a required fee. To the extent you use scholarship or fellowship funds to pay for these types of required fees and expenses, the funds should be excluded from your taxable income.

What portion of my scholarship or fellowship would be taxable? Any portion of a scholarship or fellowship used to pay for room and board, travel, moving, and other living expenses should be included in your taxable income for the year. Again, this would be the case regardless of how the funds were paid, i.e., directly to you or on your behalf. Therefore, you may have to pay income taxes on the amount of your scholarship or fellowship used for such expenses. For more information on the tax treatment of scholarships and fellowships, see **IRS Publication 970, Tax Benefits for Education**.

How will I be taxed on the portion of my scholarship or fellowship that is not tax-free? IRS regulations do not permit the University to withhold income taxes on the taxable portion of a scholarship or fellowship. Therefore, depending upon the taxable amount of your award, you may need to make estimated income tax payments prior to filing your tax return. For more information on the rules pertaining to estimated tax payments, see **IRS Publication 505, Tax**

Withholding and Estimated Tax.

Am I required to maintain any records related to my scholarship or fellowship? Yes.

Regardless of how the scholarship and fellowship funds are paid to you (i.e., either directly or on your behalf), you are required to maintain records showing that you used all or a portion of your scholarship or fellowship funds for qualifying (i.e., nontaxable) expenses. You should retain receipts and other documents that show the total amount of such expenses. You may also use your University online student billing records for this purpose. In addition, you may receive an annual tax statement from the University (see below).

FORM 1098-T, TUITION STATEMENT

The University is required to annually file a Form 1098-T information return with the IRS for most students. If a return is filed, the University must also provide a copy of the return to the student showing the information reported. Information reported on the Form 1098-T is intended to assist taxpayers in calculating the amount of the higher education tax credits or deductions they may be eligible to claim.

What information is reported on the Form 1098-T? Amounts are reported in Box 2 and Box 5 of the Form 1098-T. Box 2 represents the total Qualified Tuition and Related Expenses charged or billed to your student account for the calendar year. This amount could be different than what you actually paid for the year. Box 5 represents total Scholarships and Grants, including fellowships, from all known sources, that the University processed on your behalf. The total amount reported for these types of awards is without regard to whether any portion of an award may be taxable. You should make the determination regarding whether your scholarship or fellowship is taxable based upon your individual facts, irrespective of how the University may have applied your grant funds to the amounts you owed the University.

Are any educational loans I received reported on the 1098-T? No. Amounts reported on the Form 1098-T do not include any loans you may have received in connection with your enrollment at the University.

For more information about the education tax credits and deductions, see **IRS Publication 970**.

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