



SC REVENUE RULING #89-20

- SUBJECT:** Backup Income Tax Withholding
- EFFECTIVE DATE:** July 1, 1989
- SUPERSEDES:** S.C. Information Letter #89-19 and any oral directives in conflict herewith.
- REFERENCE:** S.C. Code Ann. Section 12-9-30 (As Amended July 1, 1989)
- AUTHORITY:** S.C. Code Ann. Section 12-3-140 (Law. Coop. 1976)
S.C. Revenue Procedure #87-3
- SCOPE:** A Revenue Ruling is the Commission's official interpretation of how tax law is to be applied to a specific set of facts. A Revenue Ruling is public information and remains a permanent document until superseded by a Regulation or is rescinded by a subsequent Revenue Ruling.
- PURPOSE:** This ruling is being issued to provide guidance on the application of Section 12-9-30 of the S.C. Code as added by the 1989 Appropriations Bill.

South Carolina backup income tax withholding is imposed on reportable payments in the same manner as provided by Internal Revenue Code Section 3406, except that the amount to be withheld is four (4) percent of the payment. S.C. Code Section 12-9-30, which requires backup income tax withholding is effective July 1, 1989.

Payors are required to deduct and withhold from payments of reportable interest and dividends, and other reportable payments a tax equal to four (4) percent of the payment if:

- (A) the payee fails to furnish his taxpayer identification number to the payor in the manner required,
- (B) the Tax Commission notifies the payor that the taxpayer identification number furnished by the payee is incorrect,
- (C) the Tax Commission notifies the payor that backup withholding should be started due to notified payee under-reporting, or

- (D) the payee fails to certify to the payor, when required, that (1) the payee is not subject to backup withholding or (2) the taxpayer identification number provided to the payor is correct.

Other reportable payments for purposes of backup withholding include certain payments of royalties, non-employee compensation and transactions by brokers and barter exchanges. The definition of "reportable interest or dividend payment", "other reportable payment" and other terms used in this Revenue Ruling are contained in section 3406 of the Internal Revenue Code.

This provision is based upon section 3406 of the Internal Revenue Code. Section 3406 and its regulations (including temporary regulations) should be consulted to determine the responsibilities of payors and payees. The following interpretations are provided to assist in applying section 3406 to South Carolina withholding on reportable payments:

1. Items (C) and (D) above only apply to reportable interest and dividend payments.
2. Only the Tax Commission or a broker who has been notified by the Tax Commission can issue the notification for items (B) or (C) above. The payor cannot begin South Carolina backup withholding if the payor is notified by the Internal Revenue Service to begin withholding under item (B) or (C). If a payor is notified to begin withholding by a broker, the payor shall not begin withholding unless the broker's notification makes it clear that:
 - a. Withholding is required by item (A) above;
 - b. Withholding has been ordered by the Tax Commission pursuant to item (B) or (C) above; or
 - c. Withholding is required by item (D) and the determination that withholding is required has been made by substituting July 1, 1989 (the effective date of the South Carolina Act) for any prior date in section 3406 and its regulations.

When a broker is required to notify a payor to begin South Carolina backup withholding, the notice must specifically indicate the condition above which has been met.

The Tax Commission intends to review lists prepared by the Internal Revenue Service to determine which payees should come within items (B) or (C) for South Carolina withholding purposes.

For purposes of item (C), the Tax Commission will not notify the payee. The Tax Commission will rely on the Internal Revenue Service to notify the payee and will not begin item (C) withholding unless the Internal Revenue Service has begun withholding.

3. If the conditions of item (A) or (D) are met, the payor should begin withholding regardless of the residence of the payee. If, however, a payor has offices in states other than South Carolina, the payor is not required to withhold under item (A) or (D) for accounts established and serviced from offices outside South Carolina.
4. In determining whether the conditions of item (A) are met, the payor will allow the payee the 60 day grace period provided by question 18 of temporary Treasury regulation 35a.9999-2 for payees who are waiting to receive their taxpayer identification numbers. Payors can allow withdrawals during this 60 day period without imposing withholding, unless the payee closes the account.
5. The payor must notify the payee that it is instituting South Carolina withholding in the same manner as it is required to notify payees about federal withholding, making the appropriate changes in the language.
6. If the Tax Commission or Internal Revenue Service notifies the payor to stop withholding, the payor must stop South Carolina withholding.
7. The payor is not required to notify the Tax Commission if it stops South Carolina withholding because it receives a termination notice from the Internal Revenue Service, the payee furnishes a new taxpayer identification number, or any other authorized reason.
8. If a payee believes that South Carolina withholding has been in- correctly ordered, or the reason for it no longer exists, the payee can request an order terminating South Carolina withholding. Requests for termination with an explanation of the reasons for it should be sent to:

PRO - Backup Withholding
P.O. Box 11189
Columbia, South Carolina 29211-1189

There is no reason to make this request if the Internal Revenue Service terminates withholding. See item 6 above.

9. Effective date - The date January 1, 1984, and all other dates prior to July 1, 1989, in section 3406 of the Internal Revenue Code and its regulations, will be deemed to be July 1, 1989, for South Carolina withholding purposes. Therefore, for example, payee certification failure ((D) above) only applies to accounts opened after July 1, 1989. Accounts opened prior to July 1, 1989, are, on or however, subject to withholding under (A) above if the taxpayer never furnished his taxpayer identification number.
10. Returns - Withholding agents are required to make a return and remit withheld funds on the last day of the month following each calendar quarter for which funds are withheld. Funds are to be paid in the same manner and to the same institution as normal wage

withholding. Form 1605, Employers Withholding Tax Return - Quarterly, and Form 1606, Employers Annual Reconciliation of Income Tax Withheld are being revised to accommodate the new law.

11. Information Returns (1099s) - Payors should include the amount of South Carolina withholding on Form 1099s or substitute Form 1099s sent to payees. If the payor uses Form 1099 and it has a block for state withholding, the amount must be included in that block. The Tax Commission is working with the Internal Revenue Service to provide that block on Form 1099s. If the payor uses Form 1099 and there is no such block, the payor should place "SC Withholding \$____" immediately under the title of the 1099. For example, under the words (Interest Income) for the interest 1099. See the attached example.

The South Carolina Tax Commission has entered into an agreement with the Internal Revenue Service to allow combined reporting of information returns on magnetic media. The requirements and procedures are outlined in Internal Revenue Procedure 83-48 under the title of "Combined Federal/State Filing".

If the payor has filed its consent to participate and participates in the Combined Federal/State Filing with the Internal Revenue Service, it is not required to send copies of Form 1099 to the Tax Commission. If the payor has not consented to Combined Federal/State Filing, it must file its information returns with the Tax Commission in accordance with section 12-7-1590 of the South Carolina Code. For 1989, these returns do not have to include South Carolina back-up withholding information.

The payee will be required to submit a copy of the Form 1099 (or substitute 1099) with his or her income tax return to obtain credit for the payments.

12. Penalties - The payor is liable for the amount which should have been withheld. In addition penalties for failure to withhold include those contained in section 12-54-40(b)(1) and (2). In the case of failure to file a return, the penalty is five percent of the amount which should have been withheld with an additional five percent for each additional month, not to exceed twenty-five percent. If the return is not filed within 60 days of the due date the addition for failure to file will not be less than the lesser of \$100 or 100% of the amount required to be shown on the return. In the case of failure to pay, the penalty is one-half of one percent with an additional one-half of one percent for each month, not to exceed twenty-five percent. If any part of an underpayment is due to negligence or disregard of regulations, a penalty of five percent of the underpayment and fifty percent of the interest payable under section 12-54-20 will be assessed. Withholding agents should be aware that these penalties may be combined if applicable.

The \$50 penalty in section 6676 of the Internal Revenue Code on payors failing to include a taxpayer identification number on a return or including an incorrect number does not apply to South Carolina withholding.

SOUTH CAROLINA TAX COMMISSION

s/S. Hunter Howard Jr.
S. Hunter Howard, Jr., Chairman

s/A. Crawford Clarkson Jr.
A. Crawford Clarkson, Jr., Commissioner

s/T. R. McConnell
T. R. McConnell, Commissioner

Columbia, South Carolina
August 23, 1989