In response to concerns about the difficulties that some foreign students are experiencing in obtaining refunds of withholding tax reported on Form 1042-S, Foreign Person’s U.S. Source Income Subject to Withholding, the IRS just completed a comprehensive review of the program. As a result, the IRS is taking steps to help foreign students at United States colleges and universities and other foreign taxpayers affected by this situation, including adjusting withholding and issuing refunds as appropriate.

No additional action is needed at this time by foreign students and other foreign taxpayers who filed Form 1040NR to request a refund of tax withheld on Form 1042-S.

Background

The IRS review found several areas that are resulting in a significant number of “false positives” in our processing systems – meaning tax returns are being selected for review and validation for issues that present minimal risk of fraudulent or erroneous refunds. While some degree of false positives is inevitable in any compliance program aimed at detecting fraud and protecting revenue, our review indicated we are not achieving the proper balance in this area. Although we initially thought the issues were caused by tax software, upon a closer review these problems were minimal and easily corrected.

Steps the IRS is taking

We are taking several actions to resolve the accounts of those taxpayers who were affected by our existing verification process and to adjust the process going forward to help avoid further issues. We are working as quickly as possible to identify all the taxpayers whose refunds are being held as a result of this process. As they are identified, we will release the hold and issue the refunds (with interest, in instances where we have exceeded the 180 calendar day period for processing these refunds).

Taxpayers whose withholding credits were denied will have their withholding restored, eliminating any balance due and thus stopping the notices of levy. Also, we will not be holding any additional refunds until we have redesigned the process in place for detecting fraudulent or questionable returns and refunds.