

Form 1042 withholding return now requires electronic filing

As we approach the year end, there is an important filing change for tax year 2023 that applies to any business that pays US sourced income to foreign persons. If your organization pays foreign individuals or entities and files the 1042-S form – you are also required to file form 1042, which is the tax return “cover letter” or consolidated statement of all payments and withholding to these foreign individuals. An important distinction between the two forms is that 1042-S forms are filed with the IRS and sent to individual payees, while the 1042 return is only filed with the IRS. Another important point is that the 1042 return is typically required whether you withheld taxes from your foreign payees or not.

Historically, the IRS has not supported the electronic filing of Form 1042. However, starting with tax year 2023 reporting, the IRS will now require financial institutions and organizations that file more than 10 information returns for the calendar year to file form 1042 electronically. Let’s take a quick look at what this means.

Who will be impacted?

Any business/firm/withholding agent that is required to issue at least [10 information returns \(including Forms 1099, W-2, 1042-S, etc.\)](#) will need to comply with the new electronic filing requirements. However, if you are doing business as an individual (Sole Proprietorship), estate or trust, this change does not apply to you.

Why is electronically filing the 1042 return such a challenge?

Apart from the fact that the 1042 is a complex return, the process of submitting the file to the IRS may be difficult for several reasons.

- First, the electronic filing of the 1042 tax return must be completed through the IRS Modernized e-File (MeF) system. Unlike the File Information Return Electronically (FIRE) System for submitting series 1099 and 1042-S forms, MeF requires additional background check requirements and a longer application process. The process for completing and submitting your application to the IRS MeF system through the IRS e-Services system could take 45 days or more.
- Second, the application process itself is complex as organizations are required to assign two responsible officers to own the account and process. These individuals must be a licensed professional in one of the following areas: attorney, bank official, CPA, EA or an officer of a publicly owned corporation. If they don’t meet one of these criteria, they will be required to go through an extensive background check, which includes a fingerprinting process. And, once your organization is approved, you will still need to build and test the MeF transmittal with the IRS to obtain final approval to file.
- Lastly, as part of this update, businesses are also required to file corrections in the same method in which the original version was filed. Like the new eFile requirements for most 1099, W-2 and 1095 series forms, any changes/corrections to Form 1042, must also be submitted electronically if the original version was filed electronically. So whatever process or provider you use, original filing and corrections will need to be supported.

What does this mean for the 945 or other 94x series forms?

The 945 and other 94x series forms are not required to be filed electronically as part of these changes. However, when determining whether the aggregate of 10 forms threshold has been met to require electronic filing, a business must include the 94x series of forms in the count.

Why is this such a big deal?

Transactions involving U.S. income and non-U.S. payees have been a Tier 1 audit focus for the IRS since the Foreign Account Tax Compliance Act (FATCA) was implemented. Per the IRS guidelines, failing to file Form 1042 electronically can trigger an IRS examination/audit of all transactions involving non-U.S. payees. Make sure to consult your tax advisor on the specific risks/implications of not filing the 1042 withholding return for your organization.

How Sovos 1099 Pro can help?

While the 1042-S Pro software and Service Bureau continue to support 1042-S filing, we do not directly support the filing of the associated 1042 withholding return for tax year 2023. Our parent company, [Sovos](#) is one of the few IRS approved Modernized e-File (MeF) Business Providers for 1042 returns. If your organization needs to electronically file the 1042 tax return, we encourage you to learn more about this turnkey service by visiting the solution page [here](#).