

**VOLUME 10, CHAPTER 6: “FEDERAL, STATE, LOCAL, AND FOREIGN TAXES”****SUMMARY OF MAJOR CHANGES**

All changes are denoted by [blue font](#).

Substantive revisions are denoted by an asterisk (\*) symbol preceding the section, paragraph, table, or figure that includes the revision.

Unless otherwise noted, chapters referenced are contained in this volume.

Hyperlinks are denoted by [bold, italic, blue, and underlined font](#).

The previous version dated [September 2017](#) is archived.

<b>PARAGRAPH</b>	<b>EXPLANATION OF CHANGE/REVISION</b>	<b>PURPOSE</b>
All	Updated hyperlinks and formatting to comply with current administrative instructions.	Revision
060202	Clarified that taking the maximum advantage of exemptions from excise taxes is a requirement.	Revision
060209.A	Clarified tax reporting for convenience checks by incorporating existing policy from Chapter 23.	Revision
060209.B	Information not relevant to tax reporting was removed.	Revision
060701.B	Added reference for IRS reporting due dates in place of specific dates to allow reader access to the most current dates.	Revision
060702.D	Deleted duplicative information already shown in 060209.A.	Revision

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## CHAPTER 6

**FEDERAL, STATE, LOCAL, AND FOREIGN TAXES**

## 0601 GENERAL

## 060101. Purpose

This chapter prescribes the financial management policy for payment of federal, state, local, and foreign taxes associated with the various types of payments addressed in this volume. It also provides the tax information reporting requirements, and associated Departmental policy, that apply to certain contract, vendor, and miscellaneous payments (including miscellaneous payments made to military and civilian employees). Tax-related policy and requirements involving Nonappropriated Fund Instrumentalities are covered in Volume 13, Chapter 7.

## 060102. Authoritative Guidance

A. Tax Information Sources. The Federal Government's right to tax exemptions depends on the applicability of federal, state, local, and foreign tax law; tax agreements with foreign countries; items being acquired; the nature of the tax; and the type of transaction. [Federal Acquisition Regulation \(FAR\) Part 29](#) identifies the general tax applications on U.S. purchases, the rights to exemptions, and the methods of claiming exemptions. More specialized information regarding the applicability of various taxes not obtainable locally may be obtained from the taxing authorities themselves or through discussions with the Component's general counsel.

B. Exemptions from Certain Federal Taxes

1. Pursuant to Title 26, United States Code (U.S.C.), [section 4293](#), the Secretary of the Treasury has exempted the Federal Government from the communications excise tax imposed by [26 U.S.C. § 4251](#) when the supplies and services are for the exclusive use of the United States, as prescribed in [FAR 29.203\(a\)](#). This does not include facilities furnished to a Government contractor. Exemptions can be made with or without the use of an exemption certificate. The installation (or issuing) contracting office is responsible for preparing tax exemption certificates.

2. Pursuant to [26 U.S.C. § 4483\(b\)](#), the Secretary of the Treasury has exempted the Federal Government from the Federal highway vehicle use tax imposed in [26 U.S.C. § 4481](#). As stated in [FAR 29.203\(b\)](#), the exemption applies whether the vehicle is owned or leased by the Federal Government.

3. [FAR 29.202](#) identifies other circumstances in which Federal manufacturers' or special-fuels excise taxes may not be imposed in contracting situations that should be recognized by the contracting officer, who then shall furnish the seller an exemption certificate.

C. Policy Hierarchy. Internal Revenue Service (IRS)-published regulations take precedence over Department of Defense (DoD) policy for the resolution of tax-related issues. Components should consult with their designated legal counsel if there are legal questions or apparent conflicts between the policy provided in this chapter and the IRS regulations. The Defense Finance and Accounting Service (DFAS) Tax Office (dfas.cco-1099@mail.mil) may also be consulted.

## 0602 RESPONSIBILITIES

### 060201. Defense Logistics Agency-Energy (DLA-Energy)

DLA-Energy is responsible for:

A. Any application for tax refunds applicable to DLA-Energy programs. If DLA-Energy supports a Federal civilian agency, then that civilian agency is responsible for collecting data needed to apply for tax refunds; and

B. Contracting for fuels, to include the use of the proper clauses concerning local tax provisions as provided in [FAR 29.4](#).

### \*060202. Military Departments and Defense Agencies

DoD Components [are required to](#) take maximum advantage of exemptions from excise taxes.

### 060203. Contracting Officer

As outlined in FAR Part 29, the contracting officer is responsible for:

- A. Inserting the appropriate tax clauses in contracts;
- B. Soliciting prices on a tax-exclusive basis when it is known that the Federal Government as a whole, or the Armed Forces within DoD, are exempt from these taxes;
- C. Contacting local and/or state taxing authorities to verify acceptance of tax exemption certificates;
- D. Working with fleet card issuers to maximize excise tax reclamations (recoupment);
- E. Ensuring that contractors are aware of and understand duty-free entry clause requirements; and
- F. Resolving tax liability or tax exemption disputes associated with DoD contracts.

## 060204. Contractors, Vendors, and Individual Payees

A. In accordance with [FAR 29.304](#), contractors, vendors, and individual payees requesting payment from a DoD Component may be required to take certain action regarding payment, nonpayment, refund, protest, or other treatment of state and local specified taxes. This action will be taken in consultation with the contracting officer and will be varied depending on the tax consequences, nature of the purchases, and applicable contract clauses. Any entitlement or disbursing office concerns regarding any contractor tax-related payment requests or refunds should be elevated to the contracting officer for resolution.

B. [Title 31, U.S.C. § 7701\(c\)](#) and [FAR 4.902](#) require all payees, subject to the U.S. Internal Revenue Code, doing business with the DoD to furnish their Taxpayer Identification Number (TIN) as defined by [26 U.S.C. § 6109](#) (which may be a Social Security Number (SSN) for individuals). Payments are not to be authorized without a TIN or SSN on record for the required payee, except as described in paragraph 060605.

C. If the contractor or another payee believes the IRS Form 1099-[MISC](#), Miscellaneous Income, IRS Form 1099-[INT](#), Interest Income, or IRS Form 1099-[C](#), Cancellation of Debt, was improperly issued or had incorrect information, they must provide written evidence for a correction to the appropriate tax office.

## 060205. Fleet Card Issuer

The Fleet Card issuer (third-party payor) is responsible for working with DLA-Energy and DFAS to maximize excise tax reclamations, as rules and procedures vary by state. Generally, states require that tax reclamations be completed after payment is made. Refer to the [GSA SmartPay](#) website for additional Fleet Card tax information.

## 060206. DFAS

For those entitlement systems managed by DFAS and Enterprise Resource Planning (ERP)-managed systems that have coordinated with DFAS (except for Defense Health Agency and U.S. Army Corps of Engineers, where responsibility has otherwise been assigned), DFAS is responsible for:

A. Computing all appropriate tax withholdings, making deposits to the U.S. Department of the Treasury (Treasury), and filing the appropriate tax documents with the IRS;

B. Paying excise taxes as appropriate;

C. Performing reclamation of Federal and state excise tax related to fuel purchases, based on data provided by either DLA-Energy or Fleet Card issuers. DFAS responsibilities for performing reclamation will include filing for the National Guard;

D. Recording any taxes recovered in the applicable accounting systems;

E. Reviewing payment information to determine if a payment is reportable under current IRS guidelines; and

F. For those entitlement or ERP systems not managed by DFAS, for which DFAS is the responsible disbursing activity, DFAS is responsible for:

1. Issuing annual instruction on requirements for submitting necessary tax reports to DFAS for distribution to the recipients; and

2. Coordinating the issuance of the hardcopy or electronic tax statements by the IRS-mandated timelines.

060207. Office of the Staff Judge Advocate or General Counsel

These offices are responsible for providing available payment data related to all settlements of personnel cases. The document forwarded to the paying office must identify the type of payment(s) represented by the settlement (for example, compensatory damages, attorney fees, or interest), as well as the dollar amount attributed to each type of payment. This information will be used to determine the proper tax reporting of the payments. These offices must also provide the information required to properly report payments to attorneys under [26 U.S.C. § 6045\(f\)](#), separate from the claims settlement payment.

060208. Third-Party Payors

Third-party payors are responsible for preparing and filing IRS Form [1099 K](#), Payment Card and Third-Party Network Transactions, for certain payments they made, even if the item(s) procured were delivered to DoD. Further, the DoD is not responsible for filing an IRS Form 1099-MISC when the covered payments are made by third-party payors.

\*060209. Convenience Check Account Holder

\* A. The convenience check account holder is responsible for tax reporting for the convenience checks they issue and for obtaining a signed [IRS Form W9](#), Request for Taxpayer Identification Number and Certification. Refer to [IRS Instructions for Form 1099-MISC](#) for more detail regarding payment types that are not reportable to DFAS. As the checks are written, the account holder must capture the following check recipient data:

1. Payee's legal name (merchant, vendor, or individual name by which taxes are filed);

2. Payee's business name. If the business is classified as a sole proprietorship, then report the business (merchant) information and provide the sole proprietor's name;

3. Payee's legal mailing address (the address used to file their taxes);

4. [Employer Tax Identification Number \(SSN or TIN\);](#)
5. Check number;
6. Check amount;
7. [Payment date](#) (date the check is written, [not the date the check is cashed](#));
8. [A brief description of the purchase;](#)
9. [Telephone number and/or email address of the merchant; and](#)
10. [Convenience check account number.](#)

\* B. [DFAS has tax reporting responsibilities for the DoD, and thus is responsible for reporting to the IRS miscellaneous income paid to vendors/contractors.](#) Additional policy concerning the use of convenience checks is contained in Chapter 23.

C. The convenience check account holder is responsible for all backup withholding actions required based on the receipt of an IRS CP2100 notice (See [IRS website – backup withholding](#)). Also see paragraph 060605 for additional information regarding backup withholding.

#### 0603 FEDERAL EXCISE TAX (FET)

##### 060301. General

Except for exemptions provided by the Internal Revenue Code as set out in FAR Part 29, the Government must pay FET on fuel purchases. If a contract does not specify that the contract price excludes FET, then assume the contract price includes the tax and pay only the contract price. If the contract price specifically excludes the tax, then FET for fuel purchases must be billed on the invoice as a separately identified item from the contracted fuel price.

##### 060302. Exemptions

Tax exemptions or refunds are available for DoD purchases of aviation fuel and off-highway use of gasoline and road diesel fuels. Whether or not an exemption is available, or a refund application is required, depends on where in the distribution chain the purchase was made and the IRS status of the seller of the fuel. See [IRS Publication \(Pub\) 510](#) for additional IRS guidance.

##### 060303. Refunds

Requests for refunds must be filed on an [IRS Form 8849](#), Schedule 1, Nontaxable Use of Fuels.



## 060304. Quarterly FET Return

A. Unless notified differently by the IRS District Director, the accounting office responsible for reporting DLA-Energy activity must prepare and submit quarterly FET returns. DLA-Energy must submit a monthly report to DFAS containing the sales to taxable customers. A return must be made using [IRS Form 720](#), Quarterly Federal Excise Tax Return, for the first calendar quarter when the tax liability is incurred and each subsequent calendar quarter until a final return is filed. Final returns must be marked “FINAL” and are applicable only when no FET is owed and reportable in future quarters. See IRS Pub 510 for additional IRS guidance.

B. IRS Form 720 contains a list of the commodities and services subject to the tax and the tax rate. This form also serves as a return for all excise taxes for which quarterly reporting is required.

C. The accounting office is responsible for preparing IRS Form 720. Instructions for preparing this form are in [IRS Instructions for Form 720](#).

1. The IRS Form 720 is due on or before April 30, July 31, October 31, and January 31.

2. Submit the original IRS Form 720 to the appropriate IRS Center; include the amount of taxes collected.

## 060305. Collections for FET

A. Collections for FET are made to deposit fund accounts. Excise taxes collected must be transferred using the most current instructions received from the IRS. Generally, transfers of excise taxes are required semi-monthly and must be made electronically to the Treasury.

B. Report the amounts of FET collected and deposited for the sale of aviation fuel other than for the exclusive use of the DoD.

## 0604 STATE AND LOCAL TAXES

## 060401. State and Local Taxes

A. In accordance with [FAR 29.302\(b\)](#), DoD Components shall assert the Government’s immunity or exemption from taxes whenever it is available, and economically feasible to do so. State statutes identify whether the tax is levied on the seller or the purchaser. The process for seeking refunds differs from state to state. Some states accept Standard Form [1094](#), [United States](#) Tax Exemption Form, some states have their own required forms, and other states require payment of the tax at the time of purchase and provide a means for seeking refunds of the tax. The contracting officer will contact the local state taxing authority to verify if they accept tax exemption certificates. A blanket-type tax exemption certificate is used to obtain a U.S. Government

exemption from state or local taxes in the case of continuing or numerous purchases from contractors. Payments of state and local taxes are supported under the following conditions:

1. When the tax is levied on the seller, the Federal Government must pay the tax as part of the purchase price unless the taxing authority provides otherwise; or

2. When the Government has, by contract, agreed to reimburse the contractor for taxes paid to a state or municipality.

B. Unless specifically stated otherwise in the contract, it is presumed that state and local taxes are included in the contract price. When there is a valid and binding contract covering the furnishing of supplies or services at fixed unit prices, and the contract contains no provision for the adjustment of such prices in the event of the imposition on the contractor of state taxes applicable thereto, there is no authority for the payment of any taxes over and above the unit price stipulated in the contract.

#### 060402. Taxes Involving Fuel Purchases

DLA-Energy is responsible for supplying applications for tax refunds on fuel purchases for both service station and bulk purchases of fuel. Contracting officers should coordinate with DLA-Energy on the applicability and reimbursement of state and local taxes pertaining to diesel fuels and gasoline purchases.

#### 060403. Leases and Purchases

In accordance with [FAR 29.302\(a\)](#), generally, purchases and leases are immune from various state and local taxes. This determination is a legal question and requires consultation with agency counsel. FAR Subpart 29.4 references the different contract clauses concerning state and local taxes that may be included in contracts on leases and rentals.

### 0605 CUSTOMS DUTIES

#### 060501. U.S. Customs Duties on Foreign Purchases

A. Duty-Free Purchases. The DoD Components can make emergency purchases of war materials abroad. This material will be admitted free of duty. The applicability of customs duties is governed by the contract and actions of the contractor and contracting officer in accordance with [FAR 25.9](#). Federal acquisition policy in FAR 25.9 states that agencies must pursue and use any exemptions allowed when the anticipated savings to appropriated funds will outweigh the administrative cost associated with processing the required documentation. Defense Federal Acquisition Regulation Supplement [225.9](#) provides more specific Departmental policy and requirements of the administrative contracting officer (ACO) in issuing duty-free entry certificates, identifying exempted supplies, and performing other formal entry and release procedures for the foreign items procured under a prime contract.

B. Payment of Custom Duties. If the importation is not determined to be duty-free, then the duty must be charged to the same appropriation/fiscal year used to fund the purchase, even though the importation and purchase may be in different fiscal years. Expired funding is available for such obligation "adjustments" as stated in Volume 3, Chapter 10. The amount due will be generated based on the classification of imports by Customs and Border Protection. Payment vouchers must be prepared to show the payment amount, annotated with the source and calculated amount of the duty, with remittance addressed to the Collector or Deputy Collector at the port of entry. However, prior to payment, the entitlement office must obtain the ACO's approval to ensure the amount of the customs duties is not already covered in the price of the contract or exemption certifications have been issued to exempt the procured items from customs duties.

060502. Customs Exemptions for American Imports and Purchases in Canada for Joint Defense Program

A. General. The Government's imports and purchases from other countries are exempt from Canadian import duties and taxes when used for joint defense projects in Canada.

B. Refund or Remission of Taxes. Goods purchased in Canada by or for the United States, or by the Canadian Commercial Corporation, are governed by concessions when U.S. funds expended are intended for joint Canadian-U.S. projects in Canada or when the goods will become and remain U.S. property. See Defence Production and Development Sharing Remission Order [Consolidated Regulations of Canada, c. 755](#). The concessions permit refund or remission in certain circumstances, including:

1. Sales taxes paid on goods other than those for resale to members of the U.S. Armed Forces or civilian personnel for private use;

2. Excise taxes, including the stamp tax on checks. Items for resale to members of the U.S. Armed Forces or civilian personnel for private use are not exempt from stamp taxes or excise taxes; and

3. Customs duties paid on import goods when used, directly consumed, processed, or attached to items or goods manufactured in Canada and sold to the U. S. Government for use with joint Canadian-U.S. projects.

0606 MISCELLANEOUS

060601. Payments in Lieu of Taxes

Issues involving the payment of taxes are complex and should be referred to the activity's servicing legal office.

A. Charges by state or local governments for services levied on Federal Government entities or their contractors, which are not imposed on residents or nonfederal tax-exempt entities, where the cost of service is borne by the general tax revenues, are the nature of a tax to which the DoD is immune.

B. A reasonable charge by a political subdivision based on the “quantum” of direct service furnished, and which is applied equally to all property tax exempt entities, is not considered a tax against the DoD, even though the services are furnished to taxpayers without a direct charge, provided the political subdivision is not required by law to furnish the service involved without a direct charge to all located within its boundaries.

C. Payments are permitted in lieu of taxes to municipalities that have lost tax revenue due to the transfer of plants to Government Components, only when authorized by the Congress. Payments in lieu of taxes are not authorized if the property transferred was never on municipality tax rolls and municipal services had never been furnished.

060602. Foreign Taxes

U. S. Government purchases in a foreign country are not exempt, in general, from taxes and custom duties when imposed by the foreign country. The Status of Forces or other government tax or trade agreements may provide exemptions. The Component’s legal counsel should be consulted regarding the applicability of these agreements to their individual circumstances. [FAR 29.402](#) provides specific clauses pertaining to foreign taxes that may be in contracts.

060603. Taxes on Arms and Ammunition

In accordance with [10 U.S.C. § 2385](#), Federal taxes may not be imposed on the sale or transfer of firearms, pistols, revolvers, shells, or cartridges when such articles are purchased with funds appropriated for a military department.

060604. Environmental Assessments

If an environmental assessment is levied by a local government, and it represents a fee, then the payment is authorized. If the assessment appears to be a tax, and its legality is questionable, then the payment is not authorized. The Component’s legal counsel should be consulted to determine whether payment should be made.

060605. Backup Withholding

A. In most instances, pursuant to [31 U.S.C. § 3325](#), DoD may not make a payment without a valid TIN and a signed IRS Form W9. If payment is appropriate without a TIN and a signed IRS Form W9, and no exception to backup withholding applies, backup withholding must occur. Backup withholding requirements are enforced on a payment-by-payment basis, regardless of payment size. When an individual or entity has not provided a TIN and a signed IRS Form W9 as described above, the backup withholding requirements, as described in 26 U.S.C. § [3406](#), are applicable. Because of the TIN requirement imposed by 31 U.S.C. § 3325, backup withholding within DoD should be extremely rare.

B. Backup withholding requirements are separate from the reporting thresholds that apply to most IRS Form 1099 reporting. Backup withholding is applied to the principal payment only, to exclude such charges as transportation charges or interest. Payments

that are not subject to reporting on the IRS Form 1099, as set forth in subparagraph 060703.B, are not subject to backup withholding.

C. The backup withholding is reported to the IRS. The paying office will generate both an IRS Form 1099-MISC, with the reporting tax withheld to the payee in box 4, and IRS [Form 945](#), Annual Return of Withheld Federal Income Tax, for the IRS. Additional guidance is available in [IRS instructions for Form 945](#), [IRS Pub 15, \(Circular E\)](#), “Employer’s Tax Guide,” and [IRS Pub 1281](#), “Backup Withholding for Missing and Incorrect Name/TIN(s).”

D. DoD activities must perform backup withholding on reportable payments when the following conditions exist:

1. The IRS informs the paying office that the payee provided an incorrect TIN and reportable payments to the payee total \$600 or more during the calendar year,
2. An information return was required concerning the payee for the preceding calendar year, or
3. Backup withholding was required from the payee for the preceding year.

#### 0607 FEDERAL TAX REPORTING

##### \*060701. General

A. At the end of each calendar year, payment or entitlement offices are required to report certain payments to the IRS. The reporting requirements are established by [26 U.S.C. § 6041](#), [26 U.S.C. § 6041A](#), 26 U.S.C. § 6045(f), [FAR 4.904](#), and current IRS instructions/guidelines. Payment or entitlement offices must provide the recipients (payees) with an IRS Form 1099 by the date specified by the IRS (See [IRS reporting due dates](#)).

\* B. There are various payments made to military members and civilian employees that are subject to IRS Form [W-2](#), Wage and Tax Statement, reporting (e.g., military award payments and medical health service providers paid under individual set-aside contracts), as prescribed in Chapter 12, paragraph 1207. Some of these payment types may require tax withholding and will be reported on the IRS Form W-2. These payments are required to be paid by the appropriate system for accurate withholdings to be applied and reported on the annual IRS Form W-2 by [the date specified by the IRS](#) (See [IRS reporting due dates](#)). Payment through a vendor pay office is only authorized if the appropriate withholdings are computed, included, and presented for payment to the vendor pay office. At the end of each calendar year, payment or entitlement offices are required to report these payments via Form W-2 according to current Social Security Administration/IRS guidelines.

\*060702. Tax Reporting

A. Each DoD Component is responsible for the preparation of an IRS Form 1099 on its contract or vendor payments for applicable services (specified in paragraph 060703) that total \$600 or more, or royalties of \$10 or more in a calendar year to a single person or business entity (partnership, sole proprietor, or corporation), unless an exception applies. For DFAS-serviced Components, DFAS will prepare, print, and distribute the hard copy of the IRS Form 1099 to the vendor/contractor/payee and forward the same information to the IRS. If an IRS Form 1099 is required to be corrected, then the paying office that maintains the underlying payment record provides the information necessary to effect the correction. If the vendor/contractor/payee believes the IRS Form 1099 was improperly issued or had incorrect information, then the recipient must provide the written evidence needed for correction.

B. Payment data in various payment systems, for the same contractor, must be consolidated to determine if an entity was paid more than \$600 for reportable payments.

C. IRS Form 1099-MISC is not required for purchase cards and centrally-billed travel paid using a government credit card.

\* D. DFAS will not make a determination of independent contractor or employee status for tax purposes when payments are made to individuals. That determination is at the discretion of the contract-issuing activity. If there is a question, then the contract-issuing activity, through its chain of command, will submit an [IRS Form SS-8](#), Determination of Worker Status for Purposes of Federal [Employment](#) Taxes and Income Tax Withholding, to the IRS Associate Chief Counsel (tax exempt and government entities) for a determination. See [IRS Pub 1779](#), “Independent Contractor or Employee,” for additional information.

060703. IRS Form 1099 Information Reporting

A. Payments Subject to Reporting. Certain contract and vendor payments are subject to IRS Form 1099 reporting in accordance with IRS regulations/guidelines.

1. General Rule. Payments are aggregated for the taxable year for:
  - a. Business entities: sole proprietors, partnerships, and corporations, with some exceptions;
  - b. Corporations providing medical and health-care services that are not otherwise exempt from taxation under [26 U.S.C. § 501\(a\)](#);
  - c. Canceled debts; and
  - d. Interest (including Prompt Payment Act) to individuals, sole proprietors, and partnerships. Corporations are exempt from reporting interest.

2. Payment for Services. Payment or compensation for services rendered, including medical or health-care services and contractual legal services, is subject to IRS Form 1099 reporting, unless the payment should be reported on an IRS Form W-2. This reporting requirement applies regardless of whether payment is issued to an individual, a sole proprietorship, a partnership or corporation. The requirement does not apply when a payment is made to a hospital or extended health-care facility that is exempt from taxation under 26 U.S.C. § 501(a) or to a hospital or extended health-care facility owned and operated by the U.S. or an agency or instrumentality of the U.S. This reporting rule also applies to payments issued to U.S. corporations, paid in U.S. dollars, for service contracts executed in foreign countries.

3. Payments for Taxable Settlements

a. Generally, payments for personnel claims, Equal Employment Opportunity actions, and grievances represent taxable income and should be reported on an IRS Form 1099, but may be reported on an IRS Form W-2 depending on the classification of the settlement categories. This includes amounts paid in settlement, damages for nonphysical injuries or sickness (such as employment discrimination or defamation), liquidated damages, and punitive damages. Amounts paid on account of personal physical injury or physical sicknesses, however, are not taxable and are not reported on an IRS Form 1099.

b. Compensatory damages received based on emotional distress or injury that are attributable to a physical injury or physical sickness are not taxable and not reported on an IRS Form 1099, to the extent that the amount paid does not exceed the amount paid for medical care for the emotional distress. Damages paid on account of emotional distress, including physical symptoms such as insomnia, headaches, and stomach disorders, which are not attributable to a specific physical injury or physical sickness, are reportable.

c. In cases where the amount to be paid to the complainant represents back pay, and the claim originates with a DoD activity whose civilians are paid by DFAS, the claim must be forwarded to a civilian pay office for payment and issuance of an IRS Form W-2. DoD activities must forward claims representing back pay to their supporting payroll office.

d. The office forwarding personnel claims as described in Chapter 12 for payment, such as taxable settlement awards, is responsible for providing information with the settlement documents that are required for tax reporting. All settlement payments are presumed to be taxable unless otherwise indicated in the settlement agreement or meet one of the specific categories that are nontaxable.

4. Gross Proceeds Paid to an Attorney. The total amount paid to an attorney for legal services, other than contractual legal services, must be reported on an IRS Form 1099 as required by 26 U.S.C. § 6045(f). The term “attorney” includes a law firm or other providers of legal services, such as a corporation. This reporting requirement applies, regardless of whether or not legal services are provided to the Government and if the attorney is the sole payee. In the case of payment by check, payment is considered to be made to the attorney or law firm if the attorney or law firm is named the sole, joint, or alternate payee. A need to issue two



IRS Form 1099s on a single payment may occur. In this case, issue an IRS Form 1099 to the complainant and another IRS Form 1099 to the attorney. Information that must be provided by the office forwarding the claim for payment includes, but is not limited to: payee name(s), payee TIN, amount paid, payee address(es), and settling activity identification.

5. Vendors in U.S. Territories. Service payments to vendors located in Puerto Rico, Guam, American Samoa, Commonwealth of the Northern Mariana Islands, and the U.S. Virgin Islands are subject to IRS information reporting.

B. Payments Not Subject to Reporting. The following classes of contract and vendor payments are not subject to IRS Form 1099 reporting:

1. Payment of bills for merchandise, transportation, freight charges, telegrams, telephone, storage, and similar charges;

2. Payments subject to reporting on an IRS Form W-2 related to compensation paid to DoD employees or service members;

3. Payments of rent, if made to a real estate agent;

4. Payments to Government employees as an allowance or reimbursement for traveling or associated expenses, including claims for damaged household goods;

5. Payments made as an award to an informer or similar payments;

6. Payments made to a Government agency, political subdivision, or instrumentality thereof; and

7. Payments to organizations that are exempt from taxation under 26 U.S.C. § 501(a).

060704. Debt Actions Subject to IRS Form 1099-C

A. Federal agencies are required to report the cancellation of each debt to an individual, sole proprietor, partnership, or corporation. The term “debt” includes the principal owed, interest, penalties, administrative costs, and fines. If, however, interest is included in the amount reported on the IRS Form 1099-C, then it must be listed separately on the form. A debt is considered to be canceled on the date that the authorized individual approves the termination of the debt-collection process.

B. The cancellation of the debt is reported on IRS Form 1099-C, regardless of whether the debtor is required to report the debt as income. A copy of the IRS Form 1099-C must be provided to the debtor by the date specified by the IRS (See [IRS reporting due dates](#)). If payment is received on a previously canceled prior year debt, then there is no requirement to file an additional or corrected IRS Form 1099-C.



## 060705. Payments to Individuals Subject to IRS Form W-2 Reporting

A. General. As discussed in Chapter 12, various payments are issued by DFAS to, or on behalf of, DoD employees and military members. Payments may be subject to tax withholding and tax reporting (Federal and state) on an IRS Form W-2.

B. Cash Awards to Military Members

1. Cash awards to military members for disclosures, suggestions, inventions, and scientific achievements are subject to the withholding of Federal and state income taxes, as cited in Volume 7A, Chapter 44, paragraph 440201. In accordance with Volume 7A, Chapter 45, paragraph 450202, cash awards are not subject to [Federal Insurance Contributions Act \(Old Age, Survivors, and Disability Insurance/Medicare\)](#) withholding. Certain Combat Zone Tax Exclusions (CZTE) may apply. Information on the CZTE is available in [IRS Pub 3](#), “Armed Forces’ Tax Guide,” and Volume 7A, Chapter 44, Withholding of Income Tax.

2. For purposes of issuing an IRS W-2, DFAS will withhold taxes and will issue an IRS Form W-2 by the date specified by the IRS (See [IRS reporting due dates](#)). See subparagraph 060701.B for additional information.

## 060706. Filing Information Returns with the IRS

A. Filing Requirements1. Forms Required

a. When filing manual (paper) IRS Form 1099s, the IRS Form [1096](#), Annual Summary and Transmittal of U.S. Information Returns, must be used to transmit and summarize payment information. It serves as a cover sheet for one or more individual reports. IRS Form 1096 is obtained through the [IRS Forms, Instructions and Pubs](#) website.

b. A separate IRS Form 1099 must be completed for each entity concerned, and all are covered by one IRS Form 1096. IRS Form 1099s are obtained through the [IRS Forms, Instructions and Pubs](#) website.

2. Distribution of Report. The IRS Form 1096 is to be filed using the address listed on the form and the IRS Form 1099 is to be filed according to [IRS Pub 1220](#), “Specifications for Electronic Filing of Forms 1097, 1098, 1099, 3921, 3922, 5498, and W-2G.”

3. Electronic Filing. The [IRS Form 4419](#), Application for Filing Information Returns Electronically (FIRE), must be used to receive IRS approval to transmit electronically. When filing 250 or more IRS Form 1099 returns in a single report, filings are done electronically and are required to be filed by the date specified by the IRS (See [IRS reporting due dates](#)). These electronic filing procedures are published annually in IRS Pub 1220.

B. Records Retention

1. Activities preparing information returns must have the ability to reconstruct the data or records used to prepare the IRS Form 1099. The data or records shall be retained for at least three calendar years, plus the current calendar year, after filing the information return. See [\*IRS General Instructions for Certain Information Returns\*](#). These records permit an audit trail that will substantiate the amount(s) reported by showing all relevant payments, to include payments from multiple contracts. The retention period for IRS Form 1099-C or backup withholding data is four calendar years after filing the information return. The issuing location must maintain a copy of information returns or be able to recreate the tax document.

2. Documentation supporting tax-related financial transactions reported in the Component's financial statements needs to be retained in accordance with Volume 1, Chapter 9. The documentation retained must be of sufficient quality to allow an independent third party, such as an auditor, to confirm the computation of the tax-related transaction posted in the accounting system and reported on the financial statements.