



Nonresident Alien Taxation

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Agenda

Identifying the Payee

- Identifying the Payee
 - Substantial Presence Test Examples
- Classifying the Income
- Sourcing the Income
- Withholding and Reporting Rules
 - Nonresident Alien FICA Exemption
- Withholding Certificates

Tax Impact of Immigration Status

Immigration status determines applicable tax residency rules, code exceptions

- Green card holder (aka Lawful Permanent Resident)
- Government-related individuals
- Students - F, J, M Students
- Teachers and Trainees - J Non-students
- Q cultural workers
- All other categories

Can also imply potential eligibility for certain treaty benefits based on purpose of visit

Determining If and How to Withhold and/or Report

Multi-step Process:

- Identify the payee (tax resident vs. tax nonresident)
- Classify the income
- Determine source of income (Secs. 861 and 862)
- Make withholding and reporting decision
 - Including getting the appropriate documentation

Identify the Payee (Tax Resident or Tax Nonresident)

Citizens and green card holders treated as tax residents for all purposes

Nonimmigrants (temporary visa holders) require annual Substantial Presence Test (SPT) to determine tax residency

The general SPT rule:

- 31 countable US days in the current calendar year, and
- 183 countable US days based on a 3-calendar-year formula
 - All of the current year's countable days
 - 1/3 of the prior year's countable days
 - 1/6 of the 2nd preceding year's countable days
- A partial day counts as one day
- Must use fractions in the computation

Identify the Payee (Tax Resident or Tax Nonresident)

SPT exceptions for exempt (from counting US days) individuals for

- A and G Foreign Government-Related Individuals
- F, J, and M Students (includes J Student Interns)
- J and Q "Teachers and Trainees" (includes all J Nonstudents and Q Cultural Visitors)
- Above categories include dependent children who
 - Are under age 21
 - Reside with the principal alien
 - Are not members of another household

Days spent out of status are NOT exempt from counting!

Identify the Payee (Tax Resident or Tax Nonresident)

Rules for F, J, M and Q status individuals

- Students are exempt from counting US days for 5 calendar years since 1985
- J Nonstudents and Q Cultural Visitors are exempt from counting US days for 2 out of the current 7 calendar years
 - 4 out of 7 years if all remuneration is from a foreign employer
- Must consider prior visits in F, J, M, or Q status in any category that included exempt from counting US days calendar years
 - Individuals can change from NRA to RA or vice versa depending on their prior visits

Identify the Payee (Tax Resident or Tax Nonresident)

Residency start date is retroactive to the first countable day in the year that the individual becomes an RA

Residency end date is deemed by the regulations to be December 31 of the last year as an RA

Special procedures for a later start date or earlier end date

- Described in IRS Pub. 519 for tax returns but not for withholding

Identify the Payee (Tax Resident or Tax Nonresident)

Tax Resident Example:

$$2018: 100\% \times 126 = 126$$

$$2017: 1/3 \times 126 = 42$$

$$2016: 1/6 \times 126 = 21$$

$$\text{Total: } 189 = \text{RA}$$

Tax residents are subject to U.S. tax on worldwide income!

Identify the Payee (Tax Resident or Tax Nonresident)

Tax Nonresident Example:

$$2018: 100\% \times 110 = 110$$

$$2017: 1/3 \times 126 = 42$$

$$2016: 1/6 \times 126 = 21$$

$$\text{Total: } 173 = \text{NRA}$$

Tax nonresidents are only subject to U.S. tax on U.S.-source income!

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Calculation Grid:

YEAR	STATUS	Actual DAYS	Exempt	Count DAYS	Factor	RESULT
2018					1.000	
2017					.333	
2016					.167	

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 1

- Individual enters the U.S. in H-1B status on January 1, 2018. He remains until June 29, 2018 (180 days), at which point he returns to his home country for the foreseeable future.
- Individual was also in the U.S. in B-1 status from July 1 through July 30, 2017 (30 days). He has indicated that he has not been in the U.S. at all other than these two visits.

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 1

YEAR	STATUS	Actual DAYS	Exempt	Count DAYS	Factor	RESULT
2018	H-1B	180	No	180	1.00	180
2017	B-1	30	No	30	.333	10
2016					.167	
					Total	190
					Ans	RA

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 2

- Individual enters the U.S. in O-1 status on January 1, 2018. He remains until April 30, 2017 (120 days).
- Individual was also in the U.S. in B-1 status for 30 days in 2017 and 60 days in 2016. He has no other prior U.S. presence.

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 2

YEAR	STATUS	Actual DAYS	Exempt	Count DAYS	Factor	RESULT
2018	O-1	120	No	120	1.00	120
2017	B-1	30	No	30	.333	10
2016	B-1	60	No	60	.167	10
Total						140
Ans						NRA

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 3

- Individual enters the U.S. in F-1 status on January 1, 2015. He remains until April 30, 2018 (120 days). He has no other prior U.S. presence.

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 3

YEAR	STATUS	Actual DAYS	Exempt	Count DAYS	Factor	RESULT
2018	F-1	120	Yes	0	1.000	0
2017	F-1	365	Yes	0	.333	0
2016	F-1	366	Yes	0	.167	0
2015	F-1	365	Yes		Total	0
					Ans:	NRA

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 4

An individual has been in the U.S. in J-1 Research Scholar three times, with no other U.S. presence:

- June 30, 2008 – July 4, 2009
- June 15, 2013 – April 10, 2014
- March 7, 2017 – July 9, 2018

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 4

YEAR	STATUS	Actual DAYS	Exempt	Count DAYS	Factor	RESULT
2018	J1/R	190	Yes	0	1.000	0
2017	J1/R	300	Yes	0	.333	0
2016					.167	
2015						
2014	J1/R	100	No		Total	0
2013	J1/R	200	No		Ans	NRA
2012						
2011						
2010						
2009	J1/R	185	Yes			
2008	J1/R	185	Yes			

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 5

Facts are the same as in prior example, except the 2013-2014 visit was as a J-1 Student:

- June 30, 2008 – July 4, 2009
- June 15, 2013 – April 10, 2014
- March 7, 2017 – July 9, 2018

Identify the Payee (Tax Resident or Tax Nonresident)

SPT Example 5

YEAR	STATUS	Actual DAYS	Exempt	Count DAYS	Factor	RESULT
2018	J1/R	190	No	190	1.000	190
2017	J1/R	300	No	300	.333	100
2016					.167	
2015						
2014	J1/S	100	Yes		Total	290
2013	J1/S	200	Yes		Ans	RA
2012						
2011						
2010						
2009	J1/R	185	Yes			
2008	J1/R	185	Yes			

Classify the Income

Why is it so important?

What can happen if I get it wrong?

- To the organization
- To the taxpayer

How do I get it right?

Compensation or something else?

If it walks like a duck and talks like a duck, sometimes it still isn't a duck!

Classify the Income

You must determine the income type in order to apply the correct tax rules

Substance controls over form!

Neither the name given a payment nor the paying system it comes from is controlling

- A scholarship requiring services to be performed is compensation
- A stipend may be either a scholarship or fellowship grant or compensation

Source the Income

The source of income, US or foreign, varies with the type of income

- Compensation for services
- Scholarship and fellowship grants
- Prizes and awards
- Royalties

Sourcing rules are at Sections 861 and 862 of tax code

Remember, source matters because NRAs are not taxed by U.S. on foreign-source income

Source the Income

The source of compensation

- Location and currency of payment are generally not controlling
- Source is determined by where the services are performed
 - In the United States = US-source
 - Outside the United States = foreign-source
- IRS provides rules in Treas. Reg. Section 1.861-4 for allocating compensation for services both in the United States and abroad

Source the Income

Foreign-source compensation

- No documentation needed if:
 - All the services performed outside US,
 - No reason to know the provider is a US citizen or resident alien, and
 - The income is not effectively connected to a US trade or business
- Best practice - Form W-8BEN (no TIN required) and document location of services in contract and payment requests

Special Exceptions - Compensation

Special tax code rules for compensation

- Section 861(a)(3) commercial traveler rule
 - Less than 90 days in the calendar year,
 - Less than \$3,000 in the aggregate, and
 - Paid by or for a foreign employer/contractor
 - = foreign-source income

- Section 872(b)(3) exception for F, J, or Q status employees if all remuneration is paid by a foreign employer
 - Doesn't apply to foreign-government employers
 - Doesn't apply to foreign grants
 - = excludable from income

Source the Income

Scholarship and fellowship grants

- US-source if
 - The grantor is a US resident and
 - The study, research, or training is in the United States
- Foreign-source if
 - The grantor is foreign or
 - The study, research, or training is outside the United States
- A grant paid by a US paying agent on behalf a foreign grantor remains foreign-source

Source the Income

Prizes and awards

- Defined in Section 74; source defined in Treas. Reg. 1.863-1(d)
- US-source if provided by a US resident
- Foreign-source if provided
 - By a foreign resident or
 - With regard to activities outside the United States undertaken in the public interest for:
 - Targeted grants and
 - Achievement awards for past activities

Source the Income

Royalties

- Based on where the property is used
- Keep separate records for property used both within and without the United States
 - Avoids having to withhold on total income
- Must differentiate between
 - Payment for use of intangible property (royalties)
 - Payment for creating intangible property (services)
 - Sale of all substantial rights in intangible property (sale proceeds)

NRA Withholding and Reporting

Taxable Wages

- Subject to graduated wage withholding
 - Special W-4 completion rules apply
 - Cannot claim “exempt”
 - Single status even if married
 - Zero or 1 withholding allowance
 - Write “Nonresident Alien” or “NRA” on line 6
 - Electronic Form W-4 must include an indicator for NRA designation
 - “Phantom gross-up” applies
 - To remove effect of the standard deduction from the wage withholding table
 - Does not apply to residents of India who are students or business apprentices
 - See IRS Publications 515 and 15 for more details
- Report on Form W-2

NRA Withholding and Reporting

Treaty-Exempt Wages

- Exempt from federal withholding assuming valid withholding certificate provided
 - 8233 for NRAs
- Report on Form 1042-S, Chapter 3 exemption code 04

NRA FICA Exception

Section 3121(b)(19) exemption

- F-1, J-1, M-1 and Q-1/Q-2 NRAs only
- Does not apply to dependents (F-2, J-2, etc.)
- Does not apply to RAs
- Begin withholding Jan. 1 of year individual will become a RA under the SPT
 - Can refund after year-end if NRA proven

NRA FICA Exception

Section 3121(b)(19) exemption for NRAs in student status covers

- All immigration-authorized employment
- Curricular or Optional Practical Training for F-1 students
- F-1 working with an EAD based on F-1 status
- Academic training for J-1 students

NRA Withholding and Reporting

Nonqualified Scholarship/Fellowship Income

- Subject to 30% federal withholding absent a treaty exemption
 - Reduced to 14% for
 - F, J, M or Q status recipients if either
 - A candidate for a degree at a qualifying educational institution OR
 - Scholarship/fellowship is paid by a 1441(b)(2) organization
- Report on Form 1042-S

Prize/Award Income

- Subject to 30% federal withholding absent a treaty exemption
 - No allowable reduction in rate
- Report on Form 1042-S

NRA Withholding and Reporting

Royalty Income

- Subject to 30% federal withholding absent a treaty exemption or reduced rate
- Report on Form 1042-S

Withholding Certificates

No withholding certificate is required if no withholding tax reduction is claimed

- But still best to collect
 - Form W-9 as a certificate of US status
 - Form W-8BEN as a certificate of foreign status

Withholding certificates for a withholding tax exemption

- Form 8233 for treaty-exempt compensation for personal services
- Form W-9 for RA exempt from tax under a treaty
- Form W-8ECI for effectively connected income
 - But cannot be used for compensation for personal services of individuals
- Form W-8EXP for income of a tax-exempt entity
- Form W-8BEN or W-8BEN-E for all other US income

TIN required in most cases

Questions?