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Practice Update

Update: IRS Provides Relief for U.S. and Non-U.S. National Non-Residents with Substantial Presence Due to the Coronavirus

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With the restrictions on travel both into and out of the U.S. as a result of the rapid spread of the coronavirus (COVID-19) pandemic, non-U.S. or non-resident individuals (NRA) have been forced to spend a significantly greater amount of time in the U.S. than they originally projected during the current year possibly causing these NRAs to become tax residents under the Internal Revenue Code.

On April 21, 2020, the IRS released Rev. Proc. 2020-20 and Rev. Proc. 2020-27 to provide relief to individuals and businesses affected by travel disruptions arising from the COVID-19 pandemic. These Revenue Procedures and the Frequently Asked Questions (FAQs) that accompanied them provide relief for NRAs who have exceeded their days of presence in the U.S. or conduct business while physically present in the United States.

1. Impact of the Substantial Presence rules prior to Rev. Proc. 2020-20

Normally, an individual who is not a U.S. citizen or lawful permanent resident is treated as a U.S. tax resident during a particular taxable year, and is thus, subject to U.S. federal income tax on a worldwide basis (unless an applicable treaty provides

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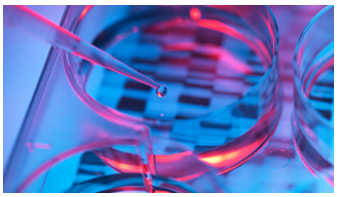

otherwise) if such individual is physically present in the U.S. for 183 days or more in the calendar year, the "Substantial Presence Test" (SPT). However, a foreign individual may also be treated as a U.S. tax resident under the SPT if the sum of (i) the number of days of his/her physical presence in the U.S. in the current calendar year, (ii) one-third (1/3) the number of days of his/her physical presence in the U.S. in the first preceding calendar year, and (iii) one-sixth (1/6) the number of days of his/her physical presence in the U.S. in the second preceding calendar year, equals or exceeds 183 days. Under this test, a person will generally not be classified as a U.S. tax resident unless he or she spends on average more than 121 days per calendar year within the U.S.

Under the medical exception, days of U.S. presence are ignored if the NRA "was unable to leave the United States because of a medical condition that arose while such individual was present in the United States." The Treasury Regulations require an NRA establish: (i) whether the NRA would have remained in the U.S. anyway if the medical problem had not occurred; and (ii) whether the medical condition arose before the NRA's arrival in the U.S. To claim the medical exception, an NRA must file Form 8843, "Statement for Exempt Individuals and Individuals with a Medical Condition", together with a statement from the NRA's U.S. physician that the NRA was indeed prevented from leaving the U.S. because of his/her condition and that "there was no indication that his/her condition ... was preexisting." If neither of these conditions apply, prior to Rev. Proc 2020-20, NRAs who exceed their days of physical presence in the U.S. as a result of the COVID-19 travel restrictions would have been deemed U.S. tax residents.

Residents of tax treaty jurisdictions earning dependent personal service or employee income in the U.S., are generally able to exclude salaries, wages and other similar remuneration derived while present in the U.S. This exclusion is available for those foreign employees who i) are present in the

U.S. for a period or periods totaling less than 183 days in the taxable year; ii) the employee's remuneration is paid by or on behalf of a non-U.S. employer; and the remuneration is not borne by a permanent establishment in the U.S. of the foreign employer. Prior to recent IRS guidance, the days of presence required for this exception would have included the days an NRA could not leave the U.S. due to the COVID-19 travel restrictions.

2. Relief provided by Rev. Proc 2020-20

Rev. Proc. 2020 specifically provides relief for NRAs who, but for COVID-19-related emergency travel disruptions, would not have been in the United States long enough to meet the SPT during 2020. Under the procedure, an NRA can exempt up to an additional sixty (60) consecutive calendar days of U.S. presence that are presumed to arise from travel disruptions caused by the COVID-19 in calculating the SPT. The COVID-19 travel restrictions will be considered a medical condition, that prevented the NRA from leaving the U.S. on each day during the 60-day period and will not be treated as a pre-existing medical condition. Further, the guidance clarifies there is a presumption a person intended to leave the U.S. but was unable to do so as a result of the COVID-19 pandemic. Note that an NRA can choose any date from February 1, 2020 to April 1, 2020 to begin counting the 60 days of exclusion.

Under Rev. Proc 2020-20, in determining an NRA's eligibility for tax treaty benefits with respect to income from employment or the performance of other dependent personal services within the United States, any days of presence during the 60-day period in which the individual was unable to leave the United States due to COVID-19, will not be counted. Therefore, in most cases residents of tax treaty countries who perform dependent personal services while present in the U.S. will be able to avoid U.S. taxation while physically present in the U.S. due to COVID-19.

The IRS provided further guidance in their FAQs with Rev. Proc. 2020-20 where employees of a foreign corporation working in the U.S. could potentially give rise to a U.S. trade or business ("USTB") or permanent establishment for their foreign employer. The FAQs clarify that services or activities conducted by an NRA employee of a foreign corporation (not otherwise engaged in a USTB) affected by the COVID-19 travel restrictions, will not be treated as engaged in a USTB as a result of such NRA's services for the 60-day relief period. The guidance further states an NRA with a tax home outside the U.S. will not create a PE for a foreign corporation for activities during their days of presence due to the COVID-19 emergency.

3. Relief Provided by Rev. Proc 2020-27

The IRS also provided relief to U.S. nationals living abroad and earning income outside the U.S. As announced in Rev. Proc. 2020-27, days spent away from the U.S. person's foreign tax home due to the COVID-19 travel restrictions will not prevent those individuals from qualifying for the foreign earned income exclusions from gross income under Sec. 911 of the Internal Revenue Code. This relief is only available to a U.S. national that reasonably expected to become a "qualified individual" for purposes of claiming the foreign earned income exclusion under section 911 but left the foreign jurisdiction during the corresponding relief period. The relief period for U.S. nationals living in China commenced on December 1, 2019. For residents of all other countries, the relief period begins February 1, 2020. This relief will expire on July 15, 2020 if not further extended.

By allowing an NRA to exclude their days of presence involuntarily caused by the COVID-19 travel restrictions, Treasury has helped alleviate the high level of anxiety felt by these "trapped visitors" to the U.S. Employees of certain foreign corporations are also relieved of the burden of creating U.S. source income for themselves or, potentially, for their employers as a result of being forced to work remotely in the U.S. Finally, U.S. nationals who

cannot return to their foreign tax homes as a result of the COVID-19 travel restrictions can also breathe a sigh of relief that they can still exclude their foreign earned income. Hopefully, the 60-day relief period offered by the IRS will be sufficient to avoid trapped visitors becoming accidental U.S. taxpayers.

Given the complexities involved with the possible tax impact of continued physical presence in the U.S. , it is essential that any NRA in danger of exceeding the number of days of physical presence in the U.S. consult with a tax adviser to properly plan for this circumstance..

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