

### **160. Non-Resident and Resident Aliens**

An entirely different set of tax rules and regulations for individuals and other entities deemed to be “nonresident aliens” exists under IRC Section 1441. In general, all income paid by the university to a foreign visitor, or to a third party on behalf of the visitor, is taxable unless the income is (i) exempt from tax under the provisions of a tax treaty between the U.S. and the person’s country of residence (IRS Publication 901), (ii) exempt from tax under a Code provision, or (iii) is “foreign source” income (IRS Revenue Ruling 89-67 states that the source of scholarship/fellowship payments is the residence of the payor.)

These restrictions should not discourage schools from inviting foreign visitors to the university/agency for short term stays; however, attention to the proper handling of payments to foreign visitors is critical.

#### *Determining Nonresident Alien/Resident Alien Classification*

In determining how to tax a non-U.S. citizen, the first question to be answered is whether the individual should be treated as a U.S. resident or a nonresident alien for federal tax purposes. There are two tests that are used to determine whether a non-U.S. citizen is an U.S. resident for tax purposes:

- the green card test, and
- the substantial presence test.

If the individual satisfies *either* test, he/she is an U.S. resident for tax purposes; if the individual satisfies *neither* test, he/she is taxed as a nonresident alien.

The green card test — An alien will be treated as a U.S. resident for tax purposes if he/she is a lawful permanent resident at any time during a calendar year (i.e. the alien has been issued an alien registration card, commonly known as a “green card”) by the Immigration and Naturalization Service.

The substantial presence test — An alien will meet this test if he/she is physically present in the United States for at least:

- 31 days during the calendar year; and
- 183 days during the three-year period that includes the current year and the two years preceding the current year.

In making the latter computation, the alien must count (i) all of the days present in the U.S. during the current year, (ii) one-third of the days present during the first preceding year, and (iii) one-sixth of the days present in the second preceding year. This test should be applied each year.

“Exempt individual” rules — If the alien is present in the U.S. under an F or J visa, those days of presence will not be counted for purposes of the substantial presence test, subject to the following limitations.

- A student F visaholder can exclude days of presence for five calendar years.
- A teacher/trainee J visaholder can exclude days of presence for two calendar years.
- The test is “calendar” years, not a consecutive time period. For example, a J visaholder who arrived in the U.S. on September 1, 2013, will be required to start counting days under the substantial presence test on January 1, 2015, since his first calendar year of exemption was 2013 and the second calendar year was 2014.

For more information regarding these rules, see IRS Treasury Regulation 301.7701(b)-1 and IRS Publication 519 ([U.S. Tax Guide for Aliens](#)).

#### *Immigration Law Restriction on Payments*

Most foreign scholars and researchers who visit the university enter the U.S. with a J-1 visa, which allows them to teach or conduct research while on campus. Most other visa types limit the nature and locations of work that can be performed by the visitor. Foreign visitors who work while they are in a visa status, which prohibits such employment, are in violation of immigration law. In some cases, advance approval must be obtained from the INS or the hosting school in order for a foreign visitor who is “sponsored” by an educational institution to be authorized to speak, lecture, or perform at another institution.

#### *Visitor for Business (and VWB, Visa Waiver for Business)*

Foreign visitors who present in the U.S. on a B-1 visa (or a waiver for business [VWB]) are prohibited from being paid any form of salary, wage, honorarium, stipend, or other form of compensation for services. The only payments that a B-1/VWB holder may receive are:

- reimbursement for expenses including accommodations, meals, and travel expenses. (Payments may be made directly to the individual or to the provider of the service. Original receipts must be supplied, subject to accountable plan restrictions found at Section 274 of the IRC); or
- fellowship or scholarship grants when the visitor does not perform services for the university/agency.
- honoraria may be paid if on campus less than a total of nine days except in the case of visa waivers (those individuals from whom visas are not required)

#### *Visitor for Tourism (and VWT, Visa Waiver for Tourism)*

Foreign visitors in the U.S. on a B-2 visa (or a waiver for tourism [VWT]) are prohibited from receiving any payment, of any kind, for any reason except for honoraria if the visitor is on campus less than a total of nine days and does not have a visa waiver.

#### *Honorariums and Travel/Expense Reimbursements*

Nonresident aliens who are invited to the U.S. for a short period of time (e.g., to participate in a weekend lecture series) often receive an honorarium and/or reimbursement of travel expenses. The IRS takes the position that such payments constitute compensation and that withholding is required unless a tax treaty provides for an exemption. Travel expenses will not be considered compensation if the expenses are properly substantiated under the accountable plan rules. However, if the nonresident alien is acting in their capacities as employees of another entity (e.g., employees of foreign universities), the foreign employer must have a reimbursement plan that meets the section 274 requirements. This payment to a nonresident alien requires an identification number (either a SSN or an ITIN). Note that resident aliens receiving expense reimbursements under an accountable plan are treated the same as U.S. citizens — the reimbursement is not compensation. (IRS Treasury Regulation 1.274-5T(h)).

### *Individual Taxpayer Identification Number (ITIN)*

Any individual who is not eligible to obtain a social security number and is required to furnish a taxpayer identifying number must apply for an IRS individual taxpayer identification number (ITIN) on Form W-7. This form may be obtained from any office of the Internal Revenue Service or any acceptance agent. The individual must make such application far enough in advance of the first required use of the ITIN to permit issuance of the number in time for compliance with such requirement.

An ITIN is required in order for a non-resident alien to receive a treaty benefit. Per Revenue Procedure 96-52, a university can act as an agent for the IRS in obtaining the ITIN, collect paper documents and submit the application. The university then receives the ITIN card to give to the student.

### *Possible Exemption from FICA Tax for Certain Visaholders*

IRC Section 3121(b)(19) provides that an individual will be exempt from FICA tax if:

- he/she is a “nonresident alien”;
- he/she is in the U.S. on an F, J, or M visa; and
- the compensation that he/she earns is related to the purpose of the visa.

The position of the IRS is that an individual who is treated as a “U.S. resident” for income tax purposes under the green card/substantial presence test discussed above will also be treated as a U.S. resident for FICA tax purposes. Therefore, many aliens who hold F, J, or M visas will nevertheless be subject to FICA tax on compensation payments made to them because they are classified as U.S. residents.

The IRS also takes the position that spouses and dependents of F, J, and M visaholders do not qualify for the IRC Section 3121(b)(19) exemption because the compensation that is paid to them is not in furtherance of the purpose for which their particular visa (the “-2” visa) was issued.

### *Income Tax Withholding Compliance*

The University is required by law to withhold tax from payments made to nonresident aliens at the following rates, unless (i) exempted by treaty, (ii) exempted by the Internal Revenue Code, or (iii) considered “foreign source” income.

- employee wages at standard graduated rates (see note below)
- fellowships & scholarships at 14% of taxable portion (IRC Section 1441(a))
- non-employee services at 30% (IRC Section 1441(a))
- reimbursement of expenses at 30%

Note: Nonresident alien employees are required to claim “single” marital status and one personal withholding allowance. These rules are modified for employees from Canada, South Korea, Mexico, and India. Refer to IRS Notice 1392 for additional details.

Almost all payments to foreign persons are potentially subject to withholding. The only categorical exceptions are

- Qualified scholarships, i.e. directly tied to instruction and achieving a degree (tuition, books and course materials, lab fees)
- Expense Reimbursements
- Payments for Goods Manufactured outside the U.S.

Due to differing tax treaties, classification is required with respect to each type of grant payment (qualified or non-qualified) to each alien.

Payment types that are subject to withholding include:

- Payments for services
- Royalties, licenses
- Prizes, awards
- Non-qualified scholarship, fellowship, stipends
- Rent

A determination of whether such payments are subject to withholding, depends on whether the payment is U.S. Sourced. If so, then it is subject to withholding.

- Services: Were services performed in U.S.?
- Prizes and Awards: Is payer of prize or award located in U.S.?
- Scholarship, Fellowship, Stipend: Is payer of *non-qualified* scholarship, fellowship, stipend located in U.S.?
- Royalties, license (software & other), reprint permission: Is all or part of the permission granted by the royalty or license exercised in the U.S.?
- Rent: Is the property of the rental payment located in U.S.?

IRS Form 8233 should be used by a nonresident alien individual claiming exemption from withholding if the exemption is based on a tax treaty between the U.S. and the nonresident alien's country of residence. If the university has received a Form 8233 that contains appropriate representations, it will not be liable for failure to withhold unless it actually knows or reasonably should know that the alien is not eligible for treaty exemption.

#### Tax Treaties

Refer to [IRS Publication 901](#) for current information on the application of tax treaties by country.

*The Payroll Office has primary responsibility for determination of taxability of expense reimbursements and should be consulted on any questionable or unclear payments.*