General U.S. Tax Structure

1. Everyone in the United States (including foreign nationals) must report income and pay taxes to the U.S. federal government tax agency, which is called the Internal Revenue Service (IRS).

2. Unlike in many countries, in the U.S., it is the individual’s responsibility to report income and pay taxes.
Taxation for Nonresident Aliens

1. Distinguish between resident aliens and nonresident aliens.
2. Understand substantial presence test for J-1 non-students.
3. Determine whether a tax treaty applies.
5. Complete the appropriate federal tax forms for the year.
Defining “Residency” & Other Terms

- The Dept. of Homeland Security’s concept of “residency” vs. the IRS’s concept of “residency”:

<table>
<thead>
<tr>
<th>DHS Law</th>
<th>IRS Law</th>
</tr>
</thead>
<tbody>
<tr>
<td>Immigrants</td>
<td>Resident aliens</td>
</tr>
<tr>
<td>Nonimmigrants</td>
<td>Nonresident aliens</td>
</tr>
<tr>
<td>Undocumented</td>
<td></td>
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<tr>
<td>(illegal aliens)</td>
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</tbody>
</table>

- Nonresident aliens pay tax on U.S. source income.
- Resident aliens pay tax on worldwide income, just like U.S. citizens.
Am I a Resident Alien or a Nonresident Alien?

- Generally, resident alien or nonresident alien status depends on the results of substantial presence test (SPT) (see next slide and chart).
- All J-1 non-students (e.g. teachers, researchers) are exempt from SPT only if they have been in the U.S. no more than 2 of the last 6 years.
- All F-1 and J-1 students are exempt from SPT only if they have been in the U.S. no more than 5 years.
- Any part of a calendar year in which a person was present in the U.S. counts as a full year for tax purposes (i.e. arrival in U.S. on Dec. 31 means present in U.S. for 1 year).
- Besides passing SPT, resident alien status could also be obtained if you received U.S. permanent residence or married a U.S. citizen or resident alien.
- Note: January 1 to July 2 = 183 days.
Comparative Analysis F-1 vs J-1 non-student

<table>
<thead>
<tr>
<th>Tax Treaty Benefits</th>
<th>Exempt Years for SPT</th>
<th>J-1 Scholars or Non-students</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>5 exempt years (years that are counted as 0 days in SPT)</td>
<td>2 exempt years in the last 6 years (continuous Window)</td>
</tr>
<tr>
<td></td>
<td>Varies by country (and specific articles for students only)</td>
<td>Varies by country (and specific articles for non-students only)</td>
</tr>
</tbody>
</table>

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<tr>
<th></th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
</table>
To Pass Substantial Presence Test (SPT)

- 31 days during the current year and

- 183 days during the 3-year period that includes the current year and the 2 years immediately before that counting:
  - current year times 1, plus
  - first preceding year times 1/3, plus
  - second preceding year times 1/6.
Substantial Presence Test (SPT) Worksheet

1. Days in the United States (any of 50 states) in 2017
   
   *If line 1 is **183 days or more**, you have met the SPT.*

2. Days in United States (any of 50 states) in 2016

3. Divide line 2 by 3

4. Days in United States (any of 50 states) in 2015

5. Divide line 4 by 6

6. Add amounts in line 1, 3, and 5

- If line 6 is **183 days or more**, you have met the SPT and **may file as a resident alien** (unless you are exempt or elect to file as a nonresident alien).

- If line 6 is **less than 183 days**, you have **not** met the SPT and must file as a nonresident alien.
Resident Alien Status through Marriage

- Nonresident spouse is treated as a resident;
- May file as resident aliens, but required to file a statement signed by both spouses;
- Required to file jointly; and
- No tax treaty benefits.
Tax Treaties

- An income tax treaty is a bilateral agreement entered into between two governments under which each country agrees to limit or modify the application of its domestic tax laws in an attempt to avoid “double taxation” of income, that is, having the same income item taxed by both countries.

5-Step Tax Treaty Review Process

1. Is there a tax treaty between the U.S. and the individual’s country of residence? (see Pub. 901)

2. Does the individual’s U.S. residency status (i.e. NRA? passed SPT?) qualify under the tax treaty for a possible tax exemption?

3. Does the primary purpose of the individual’s visit to the U.S. qualify for exemption under a particular article?

4. Is the individual being paid the type of income covered in the article?

5. Does the individual meet the specific qualifications set forth in the tax treaty article? (go over examples)
Special Tax Treaties

- **India Treaty:** Treaty benefits for a “scholar” from India are very different from those for “student”. The scholar benefit for “compensation for teaching and researching” is lost retroactively if the visit exceeds 2 years.

- **Canada Treaty:** No specific benefits for either students or visiting scholars. But article 15 of tax treaty which applies to dependent personal services, exempts all earned income if the nonresident earned no more than $10,000 in the tax year. But taxes all income if earned income is over $10,000.

- **China Treaty:** Treaty available to both nonresident and resident aliens. Scholar is exempt from tax on earned income for 3 years (in aggregate). $365 \times 3 \text{ years} = 1095 \text{ days}.$
Steps in Preparing a Tax Return

2. Decide on proper tax forms.
3. Know proper filing status: Generally, nonresident aliens must either select “single” filing status or the “married filing separate” status. See filing status box in tax return.
4. Understand “dependent” claims. Nonresident aliens can generally claim only one personal exemption.
5. No standard deduction. Only itemized deductions (e.g. state taxes, contributions, etc.) - see tax forms.
Filing as a Nonresident Alien

• Generally, tax is paid only on U.S.-source income.
• Tax treaty may exempt some income.
• Interest may be tax-free.
• Married nonresidents cannot file jointly.
• Generally, only one personal exemption is allowed.
• No dependent/child care or earned income credit permitted.
• Standard deduction not allowed (with one exception).
• Social security and Medicare taxes should NOT be withheld from “wages” (for F-1, J-1, M or Q).
Filing as a Nonresident Alien (continued)

- Itemized deductions are limited to:
  - State and local taxes withheld; or
  - Other itemized deductions, such as charitable contributions can be taken on Schedule A if filing with Form 1040NR.
  - Amount may be limited if adjusted gross income is greater than $258,250.

- Investment income (other than interest) is generally taxed at a flat 30% rate.
Filing a Tax Return

Who?
- All F, J, M, and Q status holders must file a statement to substantiate non-residence and possibly a tax return.

What?
- Form 8843 (mandatory for all nonresidents)
- Possibly Form 1040NR or 1040NR EZ
Filing a Tax Return (continued)

- When?
  - File Form 1040NR or 1040NR-EZ by April 15 (wages) or by June 17* (no wages).
  - File Form 8843 only by June 17.

- Where?
  - Internal Revenue Service Center, Austin, TX 73301-0215 (if expecting a tax refund or no taxes are due) or
  - Internal Revenue Service, P.O. Box 1303, Charlotte, N.C. 28201-1303 (if tax payment is enclosed).

* The usual deadline is June 15\(^{th}\), but in 2019, the deadline is June 17\(^{th}\) because June 15\(^{th}\) falls on a Saturday.
Can I File a 1040NR-EZ instead of a 1040NR?

- Cannot claim dependents.
- Cannot be claimed as someone’s dependent.
- Must be under 65 years of age.
- Only wages, salaries, tips, taxable refunds of state/local income taxes, & scholarships or fellowships. For all other income, use 1040NR.
- Taxable income is less than $100,000.
- Only adjustments to income are exclusions for scholarship & fellowship grants.
- Cannot claim spouse.
- Only itemized deduction is for state & local income tax.
- Cannot claim any tax credits.
Consequences of Failure to File a Tax Return

- If no taxes are owed, there’s no penalty. However, Form 8843 is always required.
- Individuals in nonimmigrant statuses (e.g. J-1, F-1, etc.) in the U.S. must not violate any U.S. laws—including tax laws.
  - The Department of Homeland Security is interested in tax compliance when an individual files for U.S. permanent residency!
Unusual Cases

- PRC
  - Teaching, 3 years, no limit
  - Studying, no limit in time, $5,000/yr

- Indonesia
  - Teaching, 2 years, no limit
  - Studying, 5 years, $3,000/yr

- France
  - Teaching, 2 years, no limit
  - Studying, 5 years, $5,000/yr
Unusual Cases (continued)

- India
  - Standard deduction and exemptions for spouse and dependents (Article 21 (2)).

- Canada
  - $10,000 dependent personal services if it does not exceed $10,000--plus much more.

- China
  - For teaching compensation, treaty benefit valid for 3 full years (365 days x 3).

- Germany, UK, & others--retroactive clauses.
Family Issues

- Few nonresident students and scholars may claim their family members as dependents.

- If you qualify (Canada, India, S. Korea, Mexico), the dependent must have a taxpayer identification number (TIN):
  - Social Security Number (SSN)
  - Individual Taxpayer Identification Number (ITIN)
Filing Status & Marital Status

- Unmarried = Single
- Married = Use one of the married statuses even if spouse not in the U.S.
- Only nonresidents from Canada, India, S. Korea, and Mexico can claim an exemption for spouse—read the rules.
Filing Status & Dependents

• Most nonresidents cannot claim their dependents—even if the dependent is a U.S. citizen.

• Only nonresidents from Canada, India, S. Korea, and Mexico can claim a deduction for dependents—read the rules.
Spouse & Dependent Reporting Obligations

- Even if no income, all F-2s and J-2s are required to file a Form 8843 every year.
  - An ITIN is recommended.

- Income from illegal employment must be reported.

- J-2s are not exempt from FICA taxes.
What’s New for 2018 Federal Tax Returns

- Most tax rates have been reduced. 2018 tax rates are 105, 12%, 22%, 24%, 32%, 35%, and 37%.
- Personal exemption suspended. You can’t claim a personal exemption for yourself, your spouse or your dependents.
- If you are resident of Canada, Mexico, or South Korea, or are a U.S. national, as you have always done you must continue to enter your residency or nationality in space on schedule OI, item A or B.
- A new item M has been added in schedule OI.
Summary

1. Do the substantial presence test (SPT) to determine if you are a nonresident alien or a resident alien.

2. Nonresident aliens only report U.S. income.

3. Double check if treaty benefit applies to you. Is it the right country? Did you reside there last?
Samples of Tax Returns

**See exercise slides**
Final Steps

• After completion, check your return to make sure it is correct. Check every line. Review your math. Check tax table to ensure correct tax is calculated.

• Sign and date your tax return.

• Attach all required forms (e.g. W-2, 1042-S) and schedules.

• Due dates:
  • April 15, 2019 if you received wages.
  • June 17, 2019 if you received only income from scholarships or other income not subject to withholding.
Final Steps (continued)

- If you will receive a tax refund, mail to:
  Internal Revenue Service
  Austin, TX  73301-0215

- If enclosing payment (tax due), mail to:
  Internal Revenue Service
  P.O. Box 1303
  Charlotte, N.C. 28201-1303
  U.S.A.

- Electronic filing for Form 1040NR only.
Summary: What to File

1. If no income from U.S., then prepare Form 8843.

2. If income from U.S. and meets filing requirements for Form 1040NR-EZ, then prepare Form 8843 and Form 1040NR-EZ.

3. If other than the above two options, then prepare Form 8843 and Form 1040NR.
Disclaimer

- This presentation is intended to provide general information on preparing a U.S. tax return.
- The University of Hawaii does not provide personal assistance with individual tax return preparation.
- Please consult with your tax advisor if you need further assistance.