

PROFESSIONAL NETWORKS

International Student and Scholar Advising



**Federal Income Tax Brochure**

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## **Federal Income Tax Brochure**

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**By: James Tenney, Judy Todd, and Robin Catmur**

### **Introduction**

This brochure is designed to offer general guidelines only for federal income tax obligations, including determining tax residency and which forms must be filed and when.

Taxes are often complicated—even for those native to the United States. There are many different kinds of taxes in the United States, and different agencies are responsible for collecting these taxes. These taxes include:

- Personal Property Tax (supports local roads and schools and is primarily a tax on ownership of a car). This yearly local tax that will vary, depending on the purchase price of the car or cars owned. Nonresidents are not exempt from this tax.
- Social Security and Medicare taxes (together called FICA). These taxes support U.S. retirees and the disabled. Nonresidents in F, J, M, or Q categories are exempt from these taxes during the time they are “non-resident aliens” for tax purposes *if* the employment being undertaken is authorized.
- City/Local Income Tax is generally required in larger metropolitan areas and may require that a tax return be filed for that locality.
- State Income Tax (only Alaska, Florida, New Hampshire, Nevada, Tennessee, Texas, and Washington do not have a state income tax). Individuals living in all other states must file a state income tax return if they receive any U.S. income while living in that state. Some states allow tax treaty exemptions similar to those available at the federal level; others do not. It is the responsibility of all taxpayers to follow the tax rules for the state in which they live. Many state Departments of Revenue have excellent Web site resources or local offices that can provide answers for taxpayers with questions about their filing obligations.
- Federal Income Tax.

### **What is Considered Income?**

Nonresidents, for tax purposes, are taxed only on their U.S. income. With a few exceptions, this means that any income received from outside the United States is not considered taxable in the United States. Residents, for tax purposes, are taxed by the United States on their income from anywhere in the world.

Sources of U.S. income may include on-campus employment, scholarships, fellowships, graduate assistantships, practical or academic training, and any compensation received for labor.

Individuals who are nonresidents for tax purposes (as discussed below) are not required to pay taxes on interest paid to them by U.S. banks.

*Note:* “Income” is not limited to wages paid to the nonresident in cash, but also includes that portion of a scholarship, fellowship, or assistantship that is applied to housing and meal expenses. The portion applied directly to tuition, fees, and books is not considered income to any student. If scholarship money is provided directly to the nonresident by check or cash, however, it is fully taxable even if the student intends to use it to pay for tuition, fees, and/or books.

### **Effectively-Connected and Not-Effectively-Connected Income**

Effectively-connected income is any income that is directly related to the US activities of the nonresident alien. Examples of this kind of income are job wages, scholarships, and independent contractor payments. This income is taxed at graduated rates according to the total amount of income.

### **Not-Effectively-Connected Income**

These types of income are not directly related to or required by the US activities of the nonresident alien. Examples of this type of income are: gambling winnings, dividend income, capital gains, and stock market investment profits. This type of income is taxed at a flat 30% rate and, unless a tax treaty exemption applies that reduces or eliminates the tax due, the nonresident taxpayer is unable to recoup that 30% tax.

### **What is a Tax Return?**

In the United States, federal income taxes are prepaid by our employer(s) based on the estimate of liability provided by the employee on the Form W-4 (usually completed by the employee at the time of hire). Since the withholding is only an estimate, employees are given a yearly opportunity to reconcile the amount taken out with how much was owed. The name of the form on which the reconciliation is made is called the “Tax Return.” The tax return is filed with the [Internal Revenue Service](#) (IRS), an agency of the U.S. government.

In some cases, filing the tax return results in a refund from the IRS because the withholding was higher than necessary. However, sometimes a taxpayer does not have enough withheld from payments and must send a payment to the IRS with his or her tax return. Occasionally, the amount taken out matches the amount due, so no money is due by either the taxpayer or the IRS. (This happens most often when a tax treaty exemption has been applied, and there is no liability on the income.)

The deadline for filing the tax return is April 15 of every year for individuals within the United States, but an extension until April 18<sup>th</sup> is available for tax year 2010 due to a Washington, D.C. holiday. Individuals filing a tax return from outside the United States have an automatic extension of time to file until June 18. However, this is NOT an extension of time to pay, so care must be taken to not encourage late filing when tax may be due. Individuals who need to file only the Form 8843 because they had no income are given until June 15 to submit their form.

### **Who Must File a Tax Return?**

All individuals in the United States who have income must file a U.S. tax return if their income is more than the personal exemption (\$3650 for tax year 2010). If taxes were withheld, the individual *may* want to file a return to claim any refund allowed, but it is not required. Tax residents usually complete Forms 1040 or 1040-EZ. Nonresidents for tax purposes must complete either Forms 1040NR-EZ or the longer 1040-NR. (See “Tax Residency Determination” below to determine which forms must be filed.)

A tax return must be filed even when no taxes are withheld from the income due a tax treaty exemption between the United States and the country of tax residence for the international visitor. Nonresidents who are married and both work must each file a U.S. tax return.

In addition to the tax return, all individuals in F, J, M, and Q immigration status who are “exempt individuals” (including spouse and children) are required to file a Form 8843 - Statement for Exempt Individuals... Filing this form does *not* mean the person is exempt from taxes, but rather that he or she is exempt from counting days of presence in the United States to determine if he or she is to be taxed as a resident or a nonresident. This form asks for certain information about immigration status. Therefore, if a nonresident alien has no income in the United States but is still within the “exempt individual” period, he or she must file the Form 8843.

### **What is a “Non-Resident” Alien?**

Two primary U.S. government agencies use the terms “Non-resident” and “Resident Alien,” but define them differently, which can be a source of significant confusion to international visitors.

- The [U.S. Immigration Service](#) (USCIS) defines a nonresident alien as someone in the United States who is not a U.S. citizen or U.S. permanent resident and who has a residence abroad he or she does not intend to abandon (i.e., he or she has not been provided authorization to live in the United States permanently).
- The IRS divides everyone into two categories for tax purposes—resident and nonresident:
  - Residents: all U.S. citizens, Lawful Permanent Residents (i.e., “green card” holders), and nonresident aliens for immigration purposes who have met the Substantial Presence Test (described below).
  - Nonresidents: all others, regardless of immigration status.

### **Determining Tax Residency**

The [Substantial Presence Test](#) (SPT) is the way the IRS determines when nonresident aliens for immigration purposes have been in the United States long enough to be considered residents for tax purposes. To pass the SPT, one must be present in the United States for a total of 183 days or more, counted over a period of three years as detailed more fully in [IRS Publication 519](#).

Those in F, J, M, and Q immigration status do not count days of physical presence during the time they are “exempt individuals.” (Remember that “exempt individual” does not mean exempt from tax, but exempt from counting days of physical presence toward the substantial presence test.) The rules for “exempt individuals” are:

- F, J, M, or Q students and their dependents are “exempt individuals” for a period of five years throughout their lifetime (going back to January 1, 1985 when tax laws changed).

- J nonstudents and their dependents are “exempt individuals” for a period of two out of every six tax years.

During the time individuals in F, J, M, and Q immigration status are “exempt individuals,” they cannot pass the 183-day SPT and will remain nonresidents for tax purposes even though they are actually present in the United States for more than 183 days. Once the period of “exempt individual” ends, days of physical presence will be counted and they may become residents for tax purposes.

### **Claiming Exemptions for Spouse and/or Children**

The **general rule** is that a nonresident alien may claim only **one** personal exemption for himself or herself, and no additional exemptions for spouse or children. There are limited exceptions to this general rule for residents of Canada, Mexico, South Korea, and India, based on tax treaties with those countries. The details of each treaty differ. See [IRS Publication 519](#) for more information.

The [IRS Web site](#) describes these exceptions as follows:

- Residents of **Canada, Mexico**, or U.S. Nationals may claim additional exemptions for spouse and dependents if:
  - the spouse had no gross income;
  - the spouse was not the dependent of another U.S. taxpayer; and
  - the dependents otherwise qualify as dependents under the normal rules (Refer to [Publication 17](#), Chapter 3).
- Residents of the **Republic of Korea** may claim additional exemptions for spouse and children if:
  - they meet the same 3 conditions shown above for residents of Canada, Mexico, and U.S. Nationals;
  - the spouse and all children claimed have lived with the taxpayer at some time during the tax year;
  - the additional deductions for spouse and children are prorated based on the ratio of the alien's U.S. income effectively connected with a U.S. trade or business to the alien's worldwide income from all sources; and
  - the additional deductions for spouse and children are limited to the extent of the alien's taxable income.
- **STUDENTS** and **BUSINESS APPRENTICES** who are residents of **India** may claim exemptions for spouse and children if:
  - the spouse had no income and cannot be claimed by another taxpayer; and
  - the children meet **ALL** dependency tests, including the citizenship/residency test. That is, the nonresident alien Indian Student cannot claim a dependency exemption for his child unless the child is a U.S. citizen or a resident alien.

To include the name of a spouse or child on the tax return requires that each have either a Social Security Number (SSN) or an Individual Taxpayer Identification Number (ITIN). Since the [Social Security Administration](#) restricts the SSN to individuals who can work, it is more likely that an ITIN will be required. The ITIN application must be sent with the tax return, according to the instructions for filing an [IRS Form W-7](#) – application for Individual Taxpayer Identification

Number. (Do not use regular address for tax returns when a Form W-7 accompanies a tax return.)

**Note:** For tax years 2005 to 2008, nonresident alien filers had been using Form 8901 to claim child tax credits for U.S. citizen children. For tax year 2009, Form 8901 has been eliminated. That means that the practice has returned to pre-2005 days, and for tax year 2009 and thereafter, only nonresidents from the above-listed four countries that are allowed to list dependents on Form 1040NR may do so.

### **Where to File and How Long to Retain Photocopies**

Photocopies of all tax returns must be kept by the taxpayer for a period of seven years, in case the IRS ever has questions regarding information provided on the tax return.

Forms 1040NR and 1040NR-EZ are mailed to:

Internal Revenue Service Center  
Austin, TX 73301-0215

All Tax Returns with Accompanying Forms W-7 (even resident returns) are mailed with the ITIN application on top of the tax return to:

Internal Revenue Service  
Austin Service Center  
ITIN Operations  
P.O. Box 149342  
Austin, TX 78714-9342

### **Where to Get Help Locally?**

A good place to start would be the International Services Office (ISO) on campus. Please note that because the primary role of the ISO is to provide immigration counsel, many offices do not have the resources, training, or institutional authority to offer direct assistance with the completion of tax returns. However, they may have information on where nonresidents can get assistance with the tax return process.

There may be what is called a [Volunteer Income Tax Assistance](#) (VITA) program located on or near campus. These programs involve volunteers who receive training from the IRS to assist others in filing federal tax returns. Most VITA programs are trained to assist with resident returns, and may have little knowledge on how to prepare a nonresident (NRA) return. Therefore, it is crucial that individuals seeking help at a VITA program identify themselves as nonresidents for tax purposes.

Sometimes there is a nonresident alien VITA site on or near the campus. These volunteers are specially trained to serve the tax return needs for nonresidents, and often are not able to provide assistance to residents for tax purposes because of the difference in the training programs. Either the campus ISO or an IRS office should know if there are VITA or NRA VITA programs available locally.

Other offices such as the university payroll office and business and law colleges may also have information about tax return preparation services for nonresidents. Local libraries often host VITA programs that are also trained to assist with filing of state income tax returns.

## **Additional Resources**

Internal Revenue Service

<http://www.irs.gov>

IRS Forms

<http://www.irs.gov/formspubs/index.html>

IRS Publications

- 515: *Withholding of Tax on Non-resident Aliens and Foreign Corporations*
  - Detailed instructions on withholding amounts and processes. Includes tax treaty tables. This is a resource more for institutions making payments to nonresidents than for individual taxpayers.

<http://www.irs.gov/publications/p515/index.html>

- 519: *U.S. Tax Guide for Aliens*
  - Explanation of the difference between “Resident” and “Non-Resident Alien” status and other topics affecting international visitors. Provides information both for nonresidents and institutions providing income to nonresidents.

<http://www.irs.gov/publications/p519/index.html>

- 901: *U.S. Tax Treaties*
  - Tables and texts that outline each current tax treaty and any retroactive clauses with older agreements. This is valuable for both nonresident aliens and institutions making payments to them. In cases that are ambiguous, the tax treaty text should be used. <http://www.irs.gov/pub/irs-pdf/p901.pdf>
- Tax treaty information can also be found at:  
<http://www.windstar.com/public/treaties.html>

4152: *Electronic Tool-Kit for Non-Resident Alien VITA Sites*

- Comprehensive guide for those seeking more detail, including scenarios and frequently asked questions. <http://www.irs.gov/pub/irs-pdf/p4152.pdf>

IRS Link and Learn Foreign Student VITA Volunteer Training and Testing (replaced IRS Publication 678-FS as of tax year 2008) [http://www.irs.gov/app/vita/foreign\\_student.jsp](http://www.irs.gov/app/vita/foreign_student.jsp)

IRS Form W-7 found at: <http://www.irs.gov/pub/irs-pdf/fw7.pdf>

IRS Substantial Presence Test found at:

<http://www.irs.gov/businesses/small/international/article/0,,id=96352,00.html>

U.S. Citizenship and Immigration Services found at: <http://www.uscis.gov/>

Social Security Administration found at: <http://www.ssa.gov/>

## **Examples of University Resources**

University of Cincinnati -- <http://www.uc.edu/international/services.html>

University of Missouri -- <http://cashiers.missouri.edu/nra.htm>

University of Tennessee Health Science Center --

<http://www.utmem.edu/international/incometax.php>