

## LB&I Process Unit

<b>Unit Name</b>	Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers	
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# Process Overview

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

This Practice Unit addresses the general process for determining if a Nonresident Alien (NRA) student, trainee, teacher or researcher is eligible to claim a treaty-based exemption on Form 1040NR or Form 1040NR-EZ for income received that is effectively connected with a U.S. trade or business (USTB). The focus of this Practice Unit is on students, trainees, teachers, and researchers who are U.S. nonresident aliens. However, as discussed later in this Unit, students, trainees, teachers, or researchers who are resident aliens may also be eligible to claim treaty-based exemptions in certain limited cases. See slides 5 and 10 for additional information.

The United States has income tax treaties (or conventions) with a number of foreign countries under which residents (but not always citizens) of those countries are taxed at a reduced rate or are exempt from U.S. income taxes on certain income, profit or gain from sources within the United States.

Many Income tax treaties include articles, commonly referred to as the Students/Trainees article and the Teachers/Researchers article, which allow students, trainees, teachers and researchers to exempt some or all of their income from U.S. tax. The Students/Trainees article typically applies to trainees or business apprentices, as well as students. The Teachers/Researchers article typically applies to teachers, professors, researchers, and visiting scholars. The extent of the benefits provided, and the conditions for being eligible for those benefits differ from one treaty to another, so it is important to review the applicable treaty provisions and Treasury Department Technical Explanations accompanying such provisions. The following is a list of some of the conditions that are commonly found in the Student/Trainee and Teacher/Researcher articles:

- **Residency Rule:** The individual must be a resident of the treaty country (as defined under the treaty) at the time the individual claims the treaty exemption or, in the case of some treaties, must have been a resident of the treaty country at the time the individual arrived in the United States. However, as discussed later in this Unit, there are treaties which allow an individual who becomes a U.S. resident alien to claim an exemption under the Student/Trainee and/or Teacher/Researcher articles.
- **Primary Purpose:** The individual claiming an exemption under the Student/Trainee article must be in the United States for the primary purpose of studying or obtaining training; individuals claiming an exemption under the Teacher/Researcher article must be in the United States for the primary purpose of teaching or doing research.

# Process Overview (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

- **Abroad Clause:** Student and trainees are generally not taxed on scholarship and fellowship payments received from sources outside the United States.
- **Once-in-a-Lifetime Clause:** Some treaties state that an individual may only claim the benefit under the particular article once. See, for example, Art. 21(5) of the U.S.-Slovak Republic Tax Treaty.
- **Retroactive Loss Clause/Cliff Effect:** A few treaties contains provisions that retroactively eliminates benefits if the allowable period in the U.S. or income amounts are exceeded as defined in the treaty. See, for example, Art. 22(1) of the U.S.- India Tax Treaty.
- **Combination Clause:** Some treaties specify that if an individual seeks benefits under two different articles (e.g. Students/Trainees article and Teachers/Researchers article) the benefits provided, in total, shall not extend for more than a total of five years or other specified period of time.
- **Not-for-Profit Clause:** Most Teacher/Researcher articles specify that the exemption from taxation only applies to income from research undertaken for the public interest. The treaty benefit is not available if the income earned is for work primarily for the private benefit of a specific person or persons.
- **Exception to the Saving Clause:** Most treaties have a saving clause that allows the U.S. to tax its citizens and residents as if the treaty had not come into effect. However, some of these treaties also have an exception to the saving clause for benefits conferred under the Student/Trainee article and/or the Teacher/Researcher article, which would allow students, trainees, teachers, and researchers to claim treaty benefits after they become U.S. residents for tax purposes, as long as they would otherwise qualify for those benefits.



**CONSULTATION:** Benefits conferred by either the Students/Trainees or Teachers/Researchers articles vary by treaty. To determine whether an individual is eligible for a treaty benefit, always review and analyze the text of the treaty as well as any contemporaneous or subsequent Protocol(s), Memoranda of Understanding, or exchanges(s) of notes between the U.S. and the treaty countries. Look up secondary resources such as the Treasury Technical Explanations, case law, IRS guidance, and relevant articles for additional references as needed. You may also seek additional guidance from the Treaties Practice Network and/or local counsel.

# Summary of Process Steps

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Process Steps

The following are general audit steps that examiners should take to determine whether or not to allow the treaty-based exemptions claimed by trainees, teachers and/or researchers.

<a href="#">Step 1</a>	Determine the taxpayer's tax residency status for treaty purposes.
<a href="#">Step 2</a>	Determine the primary purpose of the taxpayer's visit to the United States.
<a href="#">Step 3</a>	Categorize the type of income the taxpayer received and reported on the return.
<a href="#">Step 4</a>	Analyze if the taxpayer meets the qualifications specified in the treaty article.

# Step 1: Verify Taxpayer's Treaty Residency Status

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Step 1

Determine the taxpayer's tax residency status for treaty purposes.

Considerations	Resources
<p><u>Determine if the Taxpayer is a Resident of the Treaty Country</u></p> <p>To be eligible for an exemption under the Student/Trainee article or the Teacher/Researcher of a treaty that the U.S. has with a particular country, the taxpayer must be resident of that treaty country in the year that they are claiming the treaty exemption or must have been a resident of that treaty country immediately prior to arriving in the United States. Under the residence article of a treaty, an individual is a resident of a country if he or she is subject to tax as a resident under the domestic law of that country. If an individual is a resident of both the United States and the treaty country, then residence is determined under the "Tie-Breaker" rules under the residence article of the applicable treaty.</p> <p>Note: A few income tax treaties, such as those with Barbados, Hungary, and Jamaica, allow students and trainees to elect to be taxed as residents. See, e.g., Art. 18 of the U.S.-Hungary Treaty. Under the treaty with Barbados and Jamaica, an individual who makes this election cannot exempt their income from U.S. tax under the Student/Trainee article.</p> <ul style="list-style-type: none"> <li>▪ Review the specific treaty provision defining treaty residency. Residency definitions are generally found in the first few articles of the treaty.</li> <li>▪ Determine whether the individual is a U.S. resident alien or an NRA under U.S. domestic law (IRC 7701(b)).</li> </ul>	<ul style="list-style-type: none"> <li>▪ U.S. - Barbados, US.-Hungary and U.S. - Jamaica Income Tax Treaties.</li> <li>▪ IRC 7701(b)</li> <li>▪ Practice Unit - <i>Determining an Individual's Residency for Treaty Purposes</i></li> <li>▪ Form 1040-NR, Schedule OI- <i>Other Information</i></li> <li>▪ Form 8233 - <i>Exemption from Withholding on Compensation for Independent (and Certain Dependent) Servicers of a Nonresident Alien Individual</i></li> <li>▪ Pub. 519 - <i>U.S. Tax Guides for Aliens</i>, Appendix A and B</li> <li>▪ IRM 4.60.1 - <i>Exchange of Information</i></li> </ul>

# Step 1: Verify Taxpayer's Treaty Residency Status (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### [Step 1](#)

Considerations	Resources
<p><u>Determine if the Taxpayer is a Resident of the Treaty Country (Cont'd)</u></p> <ul style="list-style-type: none"> <li>▪ Determine if the individual is (or was) a resident of the treaty country under the domestic law of the treaty country.</li> <li>▪ If applicable, apply the tie-breaker rules (discussed next).</li> <li>▪ Review Schedule OI – Other Information on Form 1040NR to see if taxpayer listed the number of days he or she was present in the United States and/or information about his or her visa.</li> <li>▪ Review IDRS for taxpayer filing history and filing status.</li> <li>▪ If warranted, request the taxpayer to provide additional documents such as a certificate of residency from the treaty country.</li> <li>▪ If warranted, request information through Exchange of Information (EOI).</li> <li>▪ If available, request the taxpayer to provide a copy of Form 8233 submitted to the payer for requesting exemption from withholding, as well as any attached statements.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 4.60.1 - <i>Exchange of Information</i></li> <li>▪ Pub. 901 - <i>U.S. Tax Treaties</i></li> <li>▪ IRS.gov - <i>Tax Treaty Tables</i></li> <li>▪ Practice Unit - <i>Determining an Individual's Residency for Treaty Purposes</i></li> <li>▪ Treas. Reg. 301.7701(b)-1(b)</li> <li>▪ Treas. Reg. 301.7701(b)-1(c)</li> </ul>

# Step 1: Verify Taxpayer's Treaty Residency Status (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Step 1

Considerations	Resources
<p><u>Determine if the Taxpayer is a Resident of the Treaty Country (Cont'd)</u></p> <ul style="list-style-type: none"> <li>▪ If applicable, review the General Definitions of the income tax treaty to determine if Taxpayer is from a "Territory" or "Possession" of the country covered by the treaty.               <ul style="list-style-type: none"> <li>- Note: Commonwealth of Independent States (CIS) on the treaty tables refers to nine different European countries that comprised the former USSR, and to which the U.S.-USSR tax treaty still applies. The countries include Armenia, Azerbaijan, Belarus, Georgia, Kyrgyzstan, Moldova, Tajikistan, Turkmenistan, and Uzbekistan.</li> <li>- In addition, the U.S.- China tax treaty does not apply to residents of Hong Kong, Macau or Taiwan (a.k.a. Republic of China/ROC).</li> </ul> </li> </ul> <p><u>Tie-Breaker Rule</u></p> <p>In some instances, a taxpayer may be considered a resident of both the U.S. and the foreign treaty country. In these cases, the examiner will need to apply an income tax treaty's tie-breaker rule. Under this rule, the country of tax residency is generally determined based on a hierarchy of factors:</p> <ul style="list-style-type: none"> <li>▪ Permanent home,</li> <li>▪ Center of vital economic interests,</li> <li>▪ Habitual abode and</li> <li>▪ Nationality.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Pub. 901 - <i>U.S. Tax Treaties</i></li> <li>▪ IRS.gov - Tax Treaty Tables</li> <li>▪ Practice Unit- <i>Determining an Individual's Residency for Treaty Purposes</i></li> <li>▪ <i>Podd v. Commissioner</i> - T.C. Memo 1998-418</li> </ul>



# Step 1: Verify Taxpayer's Treaty Residency Status (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers


### [Step 1](#)

Considerations	Resources
<p><u>Tie-Breaker Rule (Cont'd)</u></p> <ul style="list-style-type: none"> <li>▪ A taxpayer who claims to be a resident of the foreign country under the tie-breaker rule must submit a Form 8833 explaining the facts to support the claim with their tax return.</li> </ul> <p><u>The Saving Clause and Exceptions to the Saving Clause</u></p> <p>Most treaties include a “saving clause” giving the U.S. the right to tax its citizens and residents as if the treaty has not come into effect. Thus, foreign nationals who become U.S. citizens or U.S. resident aliens generally cannot exempt their income from U.S. tax under a treaty. However, most treaties include exceptions to the savings clause that allow foreign nationals who became residents (but who are not citizens or lawful permanent residents of the United States) to continue to be eligible for benefits conferred under the Student/Trainee and Teacher/Researcher Articles.</p> <ul style="list-style-type: none"> <li>▪ Determine if the taxpayer is U.S. resident or NRA for the year. For an in-depth discussion and analysis on classification, refer to related Practice Units listed on the Index of Related Practice Units slide.             <ul style="list-style-type: none"> <li>– Permanent Resident (Green Card Test),</li> <li>– Resident Alien (Substantial Presence Test, First-Year Election, NRA Spouse married to a U.S. citizen or resident alien) or</li> <li>– Nonresident Alien.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ Form 8833 - <i>Treaty-Based Return Position Disclosure under IRC Section 6114 or 7701(b)</i></li> <li>▪ Practice Unit - <i>Determining an Individual's Residency for Treaty Purposes</i></li> </ul>

# Step 1: Verify Taxpayer's Treaty Residency Status (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Step 1

Considerations	Resources
<p><u>The Saving Clause and Exceptions to the Saving Clause. (cont'd)</u></p> <ul style="list-style-type: none"> <li>▪ Most treaties have a saving clause that preserves the United States' right to tax its citizens and residents on their worldwide income.</li> <li>▪ Most treaties, other than the oldest treaties with Greece and Pakistan, provide exceptions to the savings clause for Student/Trainee and Teacher/Researcher articles, which allows a resident alien who meets the substantial presence test (SPT) to continue to be eligible for benefits under those articles.</li> <li>▪ The treaties with China and the former USSR allow lawful permanent residents (i.e., green card holders) to continue to claim treaty benefits, as long as such individuals are still students, trainees, teachers, or researchers.</li> </ul> <p> <b>DECISION POINT:</b> If it is determined that the taxpayer is a not a resident of the treaty country in the year he or she is claiming the benefit, the taxpayer is not eligible for the treaty benefit. The examiner should disallow the exclusion of income claimed under the treaty, and compute the tax due as applicable under IRC 871. Otherwise, proceed to Step 2.</p>	<ul style="list-style-type: none"> <li>▪ Pub. 901 - <i>U.S. Tax Treaties</i></li> <li>▪ U.S. - Greece Income Tax Treaty, Art. II</li> <li>▪ U.S. - China Income Tax Treaty, Art. 20</li> <li>▪ U.S. - USSR Income Tax Treaty, Art. VI</li> <li>▪ PMTA 2007-00020</li> <li>▪ <i>Podd v. Commissioner</i> - T.C. Memo 1998-418</li> </ul>

# Step 2: Determine Taxpayer's Purpose of Visit

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Step 2

Determine the primary purpose of the taxpayer's visit to the United States.

Considerations	Resources
<p><u>Determine the Taxpayer's Status as a Student/Trainee or a Teacher/Researcher</u></p> <p>In general, to be eligible for an exemption under the Student/Trainee article, the taxpayer must be in the United States with the primary purpose to study or training. Similarly, to be eligible for an exemption under the Teacher/Researcher article, the taxpayer must be in the United States with the primary purpose to teach or to conduct research. Generally, primary purpose means full time engagement in the purported activities. To determine the taxpayer's primary purpose both at the beginning of the visit and during taxpayer's stay in United States, the examiner should:</p> <ul style="list-style-type: none"><li>▪ If not provided by the taxpayer already, request the taxpayer to complete and submit Form 9210, review and verify the information if necessary.</li><li>▪ Review the type of visa the taxpayer used to enter the United States. Students usually have an F-1, J-1, M-1 or Q-1 visa. Teachers usually have a J-1 visa, but in some instances they may have other nonimmigrant work visas such as an H-1B visa. The visa document usually is a good indicator of the taxpayer's primary purpose for coming to the United States.</li></ul>	<ul style="list-style-type: none"><li>▪ Form 9210 - <i>Alien Status Questionnaire</i></li></ul>

# Step 2: Determine Taxpayer's Purpose of Visit (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers


### [Step 2](#)

Considerations	Resources
<p><u>Determine the Taxpayer's Status as a Student/Trainee or a Teacher/Researcher (cont'd)</u></p> <ul style="list-style-type: none"> <li>Issue IDR and request relevant U.S. Citizenship and Immigration Services (USCIS) documents such as Form DS-2019, forms and documents issued by U.S. institutions such as school transcripts, appointment letters, scholarship/grant letters, employment contracts, etc. These documents include Form I-20 (for F-1 students) and Form I-94 (Arrival Departure Record).</li> </ul> <p><u>Determine Which Article Can Be Used to Claim Income Exemptions Based on the Individual's Primary Purpose for Being Present in the United States</u></p> <ul style="list-style-type: none"> <li>Examiner should make sure that the taxpayer is claiming benefits under the correct treaty article. Whether the taxpayer is a student, trainee, teacher, or researcher can generally be determined based on documentation from USCIS, Department of State, and/or from the taxpayer's educational institution or employer (see previous slide). If, for example, these documents indicate that the taxpayer is in the United States for the primary purpose of being a student, then the Student/Trainee article would apply.</li> </ul>	<ul style="list-style-type: none"> <li>Form I-20 - <i>Certificate of Eligibility for Nonimmigrant Student Status (F-1 visa student)</i></li> <li>Form I-94 - <i>Arrival Departure Record</i></li> <li><i>Weyts v. Comr.</i> - T.C. Memo 2003-68</li> <li>CCA 200515018</li> <li>Form DS-2019 - <i>Certificate of Eligibility for Exchange Visitor (J-1) Status</i></li> </ul>

# Step 2: Determine Taxpayer's Purpose of Visit (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### [Step 2](#)

Considerations	Resources
<p><u>Determine Which Article Can Be Used to Claim Income Exemptions Based on the Individual's Primary Purpose for Being Present in the United States (cont'd)</u></p> <ul style="list-style-type: none"> <li>- Example: An NRA student who came to the United States on a J-1 visa for the purpose of pursuing a degree in teaching and who, after graduation, participates in the Optional Practical Training (OPT) program as a teacher-in-training is still considered a student/trainee for purposes of the treaty because his OPT is part of his education/training. In this case the taxpayer would still be eligible for benefits under the Students/Trainees article. The student cannot claim a treaty benefit under the Teachers/Researchers article even though the taxpayer is engaging in teaching activities during the OPT period because the taxpayer's primary purpose for being in the United States is to study/obtain training, not to teach.</li> <li>- Example: an NRA post-doctorate with an H-1B visa may qualify for treaty benefits under the Teacher/Researchers article if he/she is working as a teacher or researcher for a public institution or non-for-profit organization.</li> </ul> <p> <b>CAUTION:</b> NRA taxpayers who enter the U.S. on F-2 or J-2 visas (spouses of F-1 or J-1 visa holders) and later change to an F-1 or J-1 visa status may be eligible for treaty benefits under the Students/Trainees article if such taxpayers demonstrate that, under all facts and circumstances, their primary purpose in the United States was to study or obtain training.</p>	<ul style="list-style-type: none"> <li>▪ <i>Kiselev v. Commissioner</i> - T.C. Summ. Op. 2018-2</li> <li>▪ <i>Bhutta v. Commissioner</i> - 145 T.C. 351 (2015)</li> </ul>

# Step 3: Categorize Types of Income

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Step 3


Categorize the type of income the taxpayer received and reported on the return.

Considerations	Resources
<p><u>Determine the Type of Income Received During the Tax Year</u></p> <ul style="list-style-type: none"> <li>▪ The taxpayer may be receiving compensation for personal services, scholarship income and/or fellowship income, or both. The scope of what is covered by each treaty differs, so you should carefully examine the relevant treaty provision(s).               <ul style="list-style-type: none"> <li>– While the Student/Trainee articles of some treaties only exempt payments for personal services earned from teaching or performing from sources outside the U.S., there are also Student/Trainee articles that provide tax benefits for scholarship and fellowship grants received from sources in the United States.</li> <li>– The Student/Trainee articles of many treaties have a limit, typically ranging from \$2,000 to \$10,000, for the amount of personal service income that can be exempt under the article.</li> <li>– Teacher/Researcher articles generally provide an exemption for compensation from research. Most Teacher/Researcher articles have a two-year time limitation, but no limitation on the amount of income that can be exempt each year.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ IRS.gov - <i>Tax Treaty Tables</i></li> <li>▪ The U.S. Model Income Tax Convention and Model Technical Explanation</li> </ul>

# Step 3: Categorize Types of Income (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### [Step 3](#)

Considerations	Resources
<p><u>Determine the Type of Income Received During the Tax Year (cont'd)</u></p> <ul style="list-style-type: none"> <li>▪ Using Treaty Table 2 as a quick reference guide/starting point to determine the benefits provided under a treaty is recommended, but always review the actual income tax treaty articles and accompanying Technical Explanations. In addition, check to see if there are any amendments or protocols to the treaty.</li> <li>▪ Review copy of Form 1042-S for proper income codes,               <ul style="list-style-type: none"> <li>– Code 19 is typically used for compensation for students /trainees during study and training.</li> <li>– Code 18 is for compensation for teachers/researchers.</li> <li>– Code 16 is for scholarship or fellowship grants.</li> </ul> </li> <li>▪ As mentioned in Step 1, request and review appointment letters, grant letters, etc.</li> <li>▪ A qualified scholarship (as defined under IRC 117) paid to a nonresident alien individual is tax free. Qualified scholarship is not subject to withholding and is not reportable on a Form 1042-S. NRA's nonqualified scholarships and fellowship grants generally will be reported on a 1042-S by U.S. payor.</li> </ul> <p> <b>CAUTION:</b> Sometimes Form 1042-S may have incorrect income code. If there are indications of error, examiner should request additional verification from the taxpayer and/or the payors. Absence of exemption code 04 on Form 1042-S.</p>	<ul style="list-style-type: none"> <li>▪ IRS.gov - <i>Tax Treaty Tables</i></li> <li>▪ Form 1042-S - <i>Foreign Person's U.S. Source Income</i></li> <li>▪ Form 1042-S Instructions</li> <li>▪ Practice Unit - <i>Determining an Individual's Residency for Treaty Purposes</i></li> <li>▪ Pub. 970 - <i>Tax Benefits for Education</i></li> <li>▪ IRC 117</li> </ul>

# Step 3: Categorize Types of Income (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### [Step 3](#)

Considerations	Resources
<p><u>Distinguish Scholarship and Fellowship Grants from Compensation for Personal Services</u></p> <p>Examiner should review relevant documents to determine whether the amounts received by an individual is a scholarship, a grant, or is compensation for personal services. Examiners should examine the Students/Trainees article of the particular treaty under which the individual is claiming benefits to see what is covered by the provision; the Student/Trainee articles of some treaties also exempt compensation earned by student/trainees while in the United States.</p> <ul style="list-style-type: none"> <li>▪ The courts use a facts-and-circumstances test to determine the primary purpose for which the payment was made. Here are some of the factors the courts have considered to determine the character of the payment:           <ul style="list-style-type: none"> <li>– Whether the payment in question was to further the education and training of the recipient or whether it was a payment for services which directly benefited the payer.</li> <li>– Whether the individual's services were directly related to the fulfillment of a contractual commitment to a specifically sponsored project.</li> <li>– Whether the individual's work was subject to supervision, time schedules, and reporting requirements.</li> <li>– Whether the university reported amounts paid on a Form W-2 or provided health and other employee benefits.</li> <li>– Whether the amounts received by the individual was unusually large compared with less generous amounts normally awarded for fellowships.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ <i>Willie v. Commissioner</i> - 57 T.C. 383, 388 (1971)</li> <li>▪ <i>Littman v. Comr.</i> - 42 T.C. 503 (1964)</li> <li>▪ <i>Bonn v. C.I.R.</i> - 34 T.C. 64 (1960)</li> <li>▪ <i>Zolnay v. Comr.</i> - 49 T.C. 389 (1968)</li> <li>▪ <i>Proskey v. Comr.</i> - 51 T.C. 918 (1969)</li> <li>▪ <i>Sarkisov v. United States</i> - 95 A.F.T.R.2d 2005-738 (2005)</li> </ul>



# Step 4: Analyze Specific Treaty Article Qualifications

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Step 4

Analyze if the Taxpayer Meets the Specific Qualifications Specified in the Treaty Article.

Considerations	Resources
<p>The Student/Trainee and Teacher/Researcher articles of many treaties set forth limitations on either the amount of income that a taxpayer can exempt each year and/or the time period for which a taxpayer can claim the exemption. There may be additional qualifications that the taxpayer needs to meet based on the specific article.</p> <p><u>Dollar Amount Limit</u></p> <ul style="list-style-type: none"> <li>▪ Generally, there is no limit in the Student/Trainee articles for scholarship or fellowship income, as well as for remittances and allowances received by students/trainees from sources outside the United States for their maintenance, education, or training, except for in the case of the U.S.-USSR Treaty.</li> <li>▪ There is usually no limit under the Teachers/Researchers article.</li> <li>▪ However, most Students/Trainees articles that exempt compensation earned by the student/trainee while in the United States limit the amount that is exempt to a certain dollar amount allowed in a calendar year.             <ul style="list-style-type: none"> <li>– The limit usually ranges from \$2,000 to \$10,000 per year. For example, the U.S.-China Treaty Article 20 (c) has a \$5,000 dollar limit. Article XV of U.S.-Canada Treaty, provides an exemption for up to \$10,000 for compensation for personal services). Generally, any payments received beyond the limit will be taxable if no other exemption applies.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ U.S. - Commonwealth of Independent States Income Tax Treaty, Art. VI(1))</li> <li>▪ U.S. - China Income Tax Treaty, Art. 20</li> <li>▪ U.S. - Canada Income Tax Treaty, Art. XV</li> </ul>

# Step 4: Analyze Specific Treaty Article Qualifications (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Step 4

Considerations	Resources
<p><u>Time Limit</u></p> <ul style="list-style-type: none"> <li>▪ Generally, Student/Trainee and Teacher/Researcher articles provide an exemption only for a certain number of years (e.g., two years) or a certain period of time (e.g., 12-month period beginning or ending in the calendar year). If the term “year” is not defined in the treaty, it means 365 consecutive days.</li> <li>▪ The time limits set forth in the Student/Trainee articles vary depending on the treaty and depending on the type of income. There is usually a time limit on compensation for service income.               <ul style="list-style-type: none"> <li>– For example, the Student/Trainee article of U.S.-Germany treaty does not limit the amount of an exemption, or the number of years during which a student can claim an exemption, for amounts a student receives from outside the United States for maintenance, education, or training.</li> <li>– However, the U.S.-Germany treaty does have a four-year limit for the exemption of up to \$9,000/year in compensation earned while in the United States, and if this time limit is exceeded, the exemption is retroactively lost for the entire period.</li> </ul> </li> <li>▪ The Teacher/Researcher articles of most treaties contain a two-year time limit, but there are some exceptions.               <ul style="list-style-type: none"> <li>– For example, Art. XII of U.S.-Greece income Tax Treaty, which provides a three-year limit.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ U.S - Germany Income Tax Treaty, Art. 20</li>   <li>▪ U.S - Greece Income Tax Treaty, Art. 19</li> </ul>

# Step 4: Analyze Specific Treaty Article Qualifications (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers


### [Step 4](#)

Considerations,	Resources
<p><u>Time Limit (cont'd)</u></p> <ul style="list-style-type: none"> <li>▪ Teacher/Researcher articles in the treaties with India, Luxembourg, Netherlands, and the United Kingdom have a retroactive loss clause/cliff effect rule, under which an individual who overstays the two-year period will lose the benefit retroactively for the entire period.               <ul style="list-style-type: none"> <li>– Example: A professor from Luxembourg who comes to the United States to teach at a U.S. college can exempt his teaching income for two years, but if his stay in the United States exceeds the 2-year limit, the exemption will be lost retroactively, including for the first two years. The examiner will need to pick up prior year returns and disallow exemptions claimed under Article 21 of the Treaty on those returns.</li> </ul> </li> <li>▪ The Student/Trainee article of the U.S.-China income tax treaty does not specify the number of years for which an individual may obtain benefits under that provision as long as the individual is a student in good standing, including the period of time the student is engaged in OPT after graduation.</li> <li>▪ To determine whether the taxpayer has exceeded the time limit, the examiner may:               <ul style="list-style-type: none"> <li>– Review the taxpayer's prior and subsequent filing history,</li> <li>– Review passport information and the taxpayer's arrival/departure record (Form 1-94).</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ U.S. - India Income Tax Treaty, Art. 22(1)</li> <li>▪ U.S. - Luxembourg Income Tax Treaty, Art. 21(2)</li> <li>▪ U.S. - Netherlands Income Tax Treaty, Art. 21(1)</li> <li>▪ U.S. - U.K. Income Tax Treaty, Art. 20A.</li> <li>▪ U.S. - China Income Tax Treaty, Art. 20</li> </ul>

# Step 4: Analyze Specific Treaty Article Qualifications (cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### [Step 4](#)

Considerations	Resources
<p><u>Additional Requirements</u></p> <p>As previously mentioned, each treaty article varies on the specific requirements for a treaty benefit, such as the requirement that the taxpayer has to work for a qualified institution. Be sure to review the treaty in detail to ensure all requirements have been met in order for the taxpayer to claim a specific treaty benefit.</p> <ul style="list-style-type: none"> <li>▪ Qualified institutions. To be eligible for the treaty exemption under Teachers/researchers articles, the taxpayer must worked for a qualified educational or research institutions, which, if not defined in the treaty, will generally has the same meaning under the laws of the contracting state whose tax is being determined.           <ul style="list-style-type: none"> <li>– Example: An individual from Poland working at U.S. hospital as research fellow is not entitled to the treaty exemption under Article 17 of U.S.-Poland treaty. A hospital does not qualified as an educational institution.</li> </ul> </li> </ul> <p> <b>DECISION POINT:</b> If the taxpayer meets all the conditions as required by the relevant treaty provision(s), accept the return as filed and issue a no change examination report. If the taxpayer does not satisfy all the conditions, consider whether other treaty articles such as the Dependent Personal Services article or the Independent Personal Services article apply.</p>	<ul style="list-style-type: none"> <li>▪ <i>Klubo-Gwiedzinska vs. Comm’r</i> - T.C. Summ. 2017-45</li> <li>▪ U.S. - Poland Income Tax Treaty, Art. 17</li> <li>▪ Treas. Regs. 1.170A-9(c)(1)</li> </ul>

# Examples of the Process

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Description

Here is an example to illustrate the general examination process discussed in this unit. The examination steps recommended in this unit are not intended to be all-inclusive nor are they mandatory steps to be followed.

### Facts

Student A came to the United States on September 1, 2012, on a F-1 visa in order to attend University B and pursue his BA degree. Student A is a Romanian citizen and was a resident of Romania at the time he came to the United States. He did not earn any income until 2015, when he had a paid summer internship. In 2016, after receiving his bachelor's degree, he worked as an intern/trainee as part of his F-1-Optional Practical Training (OPT). In Fall 2017, Student A begins graduate school with University B from September 2017 through May 2019, in order to pay for his tuition and living expenses, he works as a graduate teaching assistant on a part-time basis. His income from working as teaching assistant is \$20,000 per year. On his 2018 Form 1040-NR, Student A excluded all income he had earned from tax under Article 19 (Teachers) of U.S.-Romania Income Tax Treaty.

### Issue

Is taxpayer entitled to treaty benefits?

### Audit Steps/Considerations

Follow the general audit steps discussed earlier, to the extent applicable:

Step 1 - Verify taxpayer's treaty residency status,

Step 2 - Determine taxpayer's purpose of visit,

Step 3 - Categorize types of income,

Step 4 - Analyze specific treaty article qualifications.

# Examples of the Process (Cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Description

First of, examiner should determine Student A's status as a resident alien or nonresident alien for the year at issue, 2018. Here, Student A first came to the United States in September 2012 and has, throughout his time in the United States, been in F-1 nonimmigrant status. In general, an individual who is a F-1 nonimmigrant will be an exempt individual for purpose of Substantial Presence Test (SPT) for a period of five calendar years, and thereafter, his or her days of presence will be counted for purposes of the substantial presence test. 2012 would be considered the first year for purposes of the five-year test. As such, in 2018 (his seventh year), Student A would no longer be an exempt individual, unless he demonstrates that he does not intend to reside permanently in the United States and has substantially complied with the requirements of his F-1 visa. If Student A is able to so demonstrate, then he remains an exempt individual and a nonresident alien in 2018. If not, Student A's days of presence in 2018 would count, and he would be a resident alien under the substantial presence test. In this case, Student A should have filed a Form 1040 and reported his or her worldwide income. However, he may still be able to claim benefits under Article 19 of the U.S.-Romania Treaty because this provision is exempt from the savings clause of the treaty. See Article 4, paragraph 4 of the U.S.-Romania Treaty.

Second, the examiner should determine whether Student A was a resident of Romania at the time he arrived in the United States. To claim the treaty benefit under the U.S.-Romania Treaty, the taxpayer must be Romania resident as defined by the treaty. The examiner may request the passport and visa information.

Examiner will then examine documentation provided by the taxpayer to determine if Student A came to the United States as a teacher/researcher. Article 19 of the U.S.-Romania Treaty requires that the individual come to the United States for a period not expected to exceed two years, at the invitation by the government or by a university or other recognized educational or research institution, for the primary purpose of teaching or conducting research. It is clear in case that Student A came to the United States as a student and not for the primary purpose of teaching or conducting research. In the year at issue, Student A is also primarily a graduate student. Furthermore, Student A did not come to the United States with the expectation to only remain two years since Student A came to pursue a four-year bachelor's degree. Therefore, Student A is not eligible for benefits under Article 19.

# Examples of the Process (Cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

### Description

Examiner should then consider whether Student A is eligible for benefits under other provisions of the treaty. Here, Examiner should consider whether Student A is eligible for benefits under Article 20 (Students and Trainees). Article 20, paragraph 1, provides exemptions for certain payments derived by an individual who is present in the United States for the primary purpose of studying, doing research, or acquiring training. Payments that are exempt under Article 20 include up to \$2,000/year in compensation earned for performance of personal services. However, Article 20 also provides that an individual is entitled to benefits under Article 20 for a period not exceeding five tax years from the date of his arrival. Since Student A arrived in the U.S. on September 1, 2012, he may claim the benefit under Article 20 to exempt up to \$2,000 per taxable year for the income from personal services earned in tax years 2015 and 2016. However, he must pay U.S. income tax on the income received as a graduate teaching assistant from September 2017 through May 2019 because the income is earned in a period after five taxable years after his arrival in the United States. In addition, the taxpayer should have file Form 1040 tax return instead of Form 1040-NR for 2018 tax year if he meets SPT.

### Conclusion

TP is not eligible for exemption under either Article 19 or Article 20 in this case. All \$20,000 income received are taxable on Form 1040-NR for 2018 tax year.

The examiner should also review Student A's prior year and subsequent returns to see if he made similar treaty claims in those years and pick up these return for examination, taking into account the statute of limitation period.

# Index of Referenced Resources

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

IRC 117

IRC 871

IRC 7701(b)

Treas. Reg. 1.170A-9(c)(1)

Treas. Reg. 301.7701(b)-1

U.S. - Barbados Income Tax Treaty

U.S. - Canada Income Tax Treaty

U.S. - China Income Tax Treaty

U.S. - Commonwealth of Independent States Income Tax Treaty

U.S. - Germany Income Tax Treaty

U.S. - Greece Income Tax Treaty

U.S. - Hungary Income Tax Treaty

U.S. - Jamaica Income Tax Treaty

U.S. - Luxembourg Income Tax Treaty

U.S. - Netherlands Income Tax Treaty

U.S. - Poland Income Tax Treaty

U.S. - U.K. Income Tax Treaty



# Index of Referenced Resources (Cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

U.S. - USSR Income Tax Treaty

*Bonn v. Comr.* - 34 T.C.(1960)

*Bhutta v. Commissioner* - 145 T.C. 351 (2015)

*Escobedo v. United States* - 112 A.F.T.R.2d 2013-7005, 2013 WL 6058485 (S.D. Cal. Nov. 14, 2013)

*Kiselev v. Commissioner* - T.C. Summ. Op. 2018-2

*Klubo-Gwiedzinska vs. Comm'r* - T.C. Summ. 2017-45

*Littman v. Comr.* - 42 T.C. 503 (1964)

*Lujan v. Comm'r* - T.C. Memo 2000-365

*Podd v. Comm'r* - T.C. Memo 1998-418

*Proskey v. Comr.* - 51 T.C. 918 (1969)

*Sarkisov v. United States* - 95 A.F.T.R.2d (RIA) 738 (2005)

*Weyts v. Comr.* - T.C. Memo 2003-68

*Willie v. Commissioner* - 57 T.C. 383, 388 (1971)

*Zolnay v. Comr.* - 49 TC 389 (1968)

CCA 200515018

PMTA 2007-00020

IRM 4.60.1 - Exchange of Information

# Index of Referenced Resources (Cont'd)

## Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers

Form I-20 - *Certificate of Eligibility for Nonimmigrant Student Status*

Form I-94 - *Arrival Departure Record*

Form DS-2019 - *Certificate of Eligibility for Exchange Visitor (J-1) Status*

Form 1040-NR, Schedule OI - *Other Information*

Form 1042-S - *Foreign Person's U.S. Source Income*

Form 1042-S Instructions

Form 8233 - *Exemption from Withholding on Compensation for Independent (and Certain Dependent) Servicers of a Nonresident Alien Individual*

Form 8833 - *Treaty-Based Return Position Disclosure under IRC Section 6114 or 7701(b)*

Form 9210 - *Alien Status Questionnaire*

# Training and Additional Resources

Examining Treaty Exemptions of Income - NRA Students, Trainees, Teachers and Researchers	
Type of Resource	Description(s)
White Papers / Guidance	<ul style="list-style-type: none"> <li>▪ Pub. 901 - <i>U.S. Tax Treaties</i></li> <li>▪ Pub. 4011 – <i>VITA/TCE Foreign Students and Scholars volunteer Resource Guide</i></li> </ul>
Podcasts / Videos	<ul style="list-style-type: none"> <li>▪ LB&amp;I FY 2016 CPE - <i>Individual Eligible for Treaty Benefits CPE</i></li> <li>▪ LB&amp;I FY 2014 CPE - <i>Taxation of Nonresident Alien Individuals</i></li> </ul>
Databases / Research Tools	<ul style="list-style-type: none"> <li>▪ IRS.gov - <i>United States Income Tax Treaties - A to Z</i></li> </ul>
Reference Materials – Treaties	<ul style="list-style-type: none"> <li>▪ Pub. 519, <i>US. Tax Guide for Aliens</i></li> <li>▪ Pub. 515, <i>Withholding of Tax on Nonresident Aliens and Foreign Entities</i></li> <li>▪ Pub. 4152, <i>Electronic Toolkit for Nonresident Alien VITA/TCE Sites</i></li> <li>▪ BNA Tax Management Portfolios 914-2<sup>nd</sup>:- <i>U.S. Income Taxation of Foreign Students, Teachers and Researchers</i></li> </ul>

# Glossary of Terms and Acronyms

Term/Acronym	Definition
CCA	Chief Counsel Advice
CIS	Commonwealth of Independent States
ECI	Effectively Connected Income
FDAP	Fixed, Determinable, Annual, or Periodical
IDR	Information Document Request
IDRS	Integrated Data Retrieval System
IRC	Internal Revenue Code
IRM	Internal Revenue Manual
NRA	Nonresident Alien
OPT	Optional Practical Training
PMTA	Chief Counsel Program Manager's Tax Advice
SPT	Substantial Presence Test
Treaty (or tax treaty)	Bilateral income tax agreement between U.S. and another country
USCIS	U.S. Citizenship and Immigration Services
USTB	U.S. Trade or Business

# Index of Related Practice Units

<b>Associated UIL(s)</b>	<b>Related Practice Unit</b>
9431	<i>Determining Tax Residency Status of Lawful Permanent Residents</i>
9431.01-03	<i>Substantial Presence Test</i>
9441.01	<i>Identification of a U.S. Trade or Business of a Nonresident Alien</i>
9441.02-01	<i>Effectively Connected Income (ECI)</i>
9441-02-01	<i>Source of Income for Nonresident Alien Individuals</i>
9441.02-01	<i>Taxation of Scholarships and Fellowship Grants</i>
9450.01	<i>Treaty Exemption of Income from Teaching</i>
9450.05	<i>Determining an Individual's Residency for Treaty Purposes</i>