

LB&I International Practice Service Process Unit – Audit

Shelf		Individual Outbound		
Volume	9	Jurisdiction to Tax Outbound (Individual Outbound)	UIL Code	9431
Part	9.1	Determination of Residency Status	Level 2 UIL	9431.01
Chapter	9.1.1	Substantial Presence Test	Level 3 UIL	9431.01-01
Sub-Chapter	N/A	N/A		

Unit Name	Substantial Presence Test
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Document Control Number (DCN)	JTO/9431.01_03(2013)
Date of Last Update	08/28/14

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Table of Contents

(View this PowerPoint in "Presentation View" to click on the links below)

[Process Overview](#)

[Determination of Process Applicability](#)

[Summary of Process Steps](#)

[Process Steps](#)

[Other Considerations and Impacts to Audit](#)

[Glossary of Terms and Acronyms](#)

[Index of Related Issues](#)

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Process Overview

Substantial Presence Test

Process Description

The purpose of this unit is to determine whether an individual meets the Substantial Presence Test (SPT) and must file a Form 1040.

Certain days of presence in the U.S. may not count for purposes of the SPT, such as days spent in the U.S. due to a medical condition that arose while in the U.S.

A person who meets the Substantial Presence Test is generally treated as a resident alien for U.S. income tax purposes ; however, there are special circumstances in which such a person may be taxed as a nonresident alien.

It is important to note that the rules for determining if an individual is a U.S. resident do not override tax treaty definitions of residency. If the taxpayer is a dual-resident under the tax laws of both the U.S and another country, the taxpayer can still claim benefits under an income tax treaty.

Many treaties contain residency tie-breaker provisions that may make an individual a nonresident of the U.S. even though that individual meets the SPT.

Example Circumstances Under Which Process Applies

- An examiner receives a case involving an individual who was physically present in the United States during the year(s) in question and must determine whether the individual has properly filed the appropriate tax return(s).

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Determination of Process Applicability

Substantial Presence Test		
An individual who meets the SPT for the calendar year is generally treated as a resident alien for U.S. income tax purposes.		
Criteria	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Physically present in the United States at any time during the day on at least 31 days during the year in question and 183 days during the 3-year period that includes the year in question and the 2 years immediately before that, counting: <ul style="list-style-type: none"> – all days present in the U.S. in the year in question, and – 1/3 of days present in the U.S. in the first year before the year in question, and – 1/6 of days present in the U.S. in the second year before the year in question. ▪ NOTE: Even if the numeric test is met, an individual is may not be considered a resident alien if certain exceptions apply. 	<ul style="list-style-type: none"> ▪ Form 1040 and/or Form 1040NR ▪ IRC § 7701(b) ▪ Treas. Reg. § 301.7701(b)-1 	
<p>NOTE: If an individual has not met the SPT, he or she may still be considered a resident alien for U.S. tax purposes if he or she is an Lawful Permanent Resident (LPR) or made a First-Year Election under IRC § 7701(b)(4). See “Residency Status of Lawful Permanent Residents” and “First-Year Election” Practice Units.</p>	<ul style="list-style-type: none"> ▪ IRC §§ 7701(b)(1)(A)(i) and (2)(A)(ii) ▪ IRC §§ 7701(b)(1)(A)(iii), (2)(A)(iv) and (4) ▪ Treas. Reg. § 301.7701(b)-4(c)(3) ▪ DCN:JTO/9431.01_02(2013) ▪ DCN:JTO/9431.01_xx(201x) 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Determination of Process Applicability (cont'd)

Substantial Presence Test		
An individual who meets the SPT for the calendar year is generally treated as a resident alien for U.S. income tax purposes.		
Criteria	Resources	6103 Protected Resources
<p>NOTE: If an individual is a nonresident alien who is married to a U.S. citizen or resident alien, the individual may be treated as a resident alien for U.S. tax purposes if he or she made a joint election with his or her spouse to be treated as a resident of the U.S.</p> <p>See the “6013(g) and (h)” Practice Units.</p>	<ul style="list-style-type: none"> ▪ IRC §§ 6013(g) and (h) ▪ Treas. Reg. §§ 1.6013-6 and 1.6013-7 ▪ DCN:JTO/9431.01_xx(201x) 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Summary of Process Steps


Substantial Presence Test	
Step 1	Determine whether the individual met the Substantial Presence Test.
Step 2	If a year in question is the year of arrival and/or departure, determine the residency start and/or termination date.
Step 3	Determine whether the individual has filed the appropriate tax return(s).


Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Step 1

Substantial Presence Test

Step 1: Determine whether the individual met the SPT.

 **DECISION POINT:** Did the individual meet the required number of days present in the U.S. the SPT? If so, determine whether an exception applies.

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Determine the number of days the individual was physically present in the U.S. For purposes of the SPT, do not count any of the following: <ul style="list-style-type: none"> Days as an exempt individual. An exempt individual is a: <ul style="list-style-type: none"> - Foreign government-related individual temporarily in the U.S. - Teacher, trainee or student temporarily present in the U.S. who substantially complies with visa requirements - Professional athlete temporarily in the U.S. to compete in a charitable sports event Days in the U.S. due to a medical condition that arose while in the U.S. Days in the U.S. less than 24 hours while in transit between two places outside the U.S. including travel between U.S airports to change planes en route to a foreign destination. 	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(5) ▪ Treas. Reg. § 301.7701(b)-3(b) ▪ Form 8843, <i>Statement for Exempt Individuals and Individuals with a Medical Condition</i> ▪ IRC § 7701(b)(3)(D) ▪ Treas. Reg. §§ 301.7701(b)-3(a)(2) and (c) ▪ Treas. Reg. § 301.7701(b)-8(a)(2) ▪ IRC § 7701(b)(7)(C) ▪ Treas. Reg. § 301.7701(b)-3(a)(3) ▪ Treas. Reg. § 301.7701(b)-3(d) 	
<p> CAUTION: A person is not considered to be in transit if that person attended a business meeting while in the U.S., even if the meeting was held at the airport.</p>		

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Step 1 (cont'd)

Substantial Presence Test

Step 1: Determine whether the individual met the SPT.



DECISION POINT: Did the individual meet the days of presence for the SPT? If so, determine whether an exception applies.

Considerations	Resources	6103 Protected Resources
<p>Days as a regular commuter from Canada or Mexico</p> <p>Days in the U.S. as a regular crew member of a foreign vessel engaged in transportation between the U.S. and a foreign country or U.S. possession, UNLESS the person otherwise engaged in any trade or business in the U.S. on those days.</p>	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(7)(B) ▪ Treas. Reg. § 301.7701(b)-3(a)(4) ▪ IRC § 7701(b)(7)(D) 	
<ul style="list-style-type: none"> ▪ Calculate the number of days the individual was physically present in the U.S – to meet the substantial presence test the individual must be present in the U.S. on at least: <ul style="list-style-type: none"> ▪ 31 days during the year in question, and ▪ 183 days during the 3-year period that includes the year in question and _____ years immediately before that, counting: <ul style="list-style-type: none"> - All days present in the year in question, and - 1/3 of days present in the first year before the year in question, and - 1/6 of days present in the second year before the year in question 	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(3)(A) 	



CAUTION: The term United States does not include U.S. possessions and territories or U.S. airspace.

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Step 1 (cont'd)

Substantial Presence Test

Step 1: Determine whether the individual met the SPT.




DECISION POINT: Did the individual meet the days of presence for the SPT? If so, determine whether an exception applies

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Determine whether an exception applies – an individual who meets the SPT may still be treated as a nonresident alien under the closer connection exception if the individual: <ul style="list-style-type: none"> - was present in the U.S. for the year at issue for fewer than 183 days, <u>and</u>, - had a tax home (as defined in IRC §911(d)(3)) in a foreign country, <u>and</u>, - maintained more significant contacts with a foreign country than with the U.S. 	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(3)(B) ▪ IRC § 911 (d)(3) ▪ Treas. Reg. § 301.7701(b)-8(a)(1) ▪ Treas. Reg. § 301.7701(b)-2 ▪ Form 8840, <i>Closer Connection Exception Statement for Aliens</i> 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Step 1 (cont'd)

Substantial Presence Test		
Step 1: Determine whether the individual met the SPT.		
 DECISION POINT: Did the individual meet the days of presence for the SPT? If so, determine whether an exception applies		
Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Consider the effect of Tax Treaties - <p>T TREATY IMPLICATION: An individual may be a tax resident of both the U.S. and a country with which the United States has an income tax treaty (sometimes referred to as a “dual-resident” taxpayer). If so, the individual might be eligible to be treated as a resident of the other country under the residency “tiebreaker” rules of the treaty with respect to that taxable year (or portion thereof) during which the person was considered a dual-resident taxpayer.</p> <p>A dual-resident taxpayer may also elect not to be treated as a nonresident alien pursuant to the rules of an income tax treaty and to file returns as a resident alien, i.e., Form 1040.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. § 301.7701(b)-7 ▪ Form 1040NR ▪ Form 8833, <i>Treaty-Based Return Position Disclosure Under Section 6114 or 7701(b)</i> ▪ Treas. Reg. § 301.7701(b)-7(e), Example 4 ▪ Form 1040 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Step 2

Substantial Presence Test

Step 2: If a year in question is the year of arrival and/or departure, determine the residency start and/or termination date.



DECISION POINT: Did the individual arrive in the U.S. in a year under examination? If so, determine the **residency start** date.

Considerations	Resources	6103 Protected Resources
<p>If the individual was not a resident alien for any part of the preceding calendar year, the residency start date is the first day during the calendar year on which the individual was physically present in the U.S. If the individual also met the lawful permanent resident (LPR) test for that year, however, the residency start date is the earlier of (1) the first day of presence in the U.S. under the SPT or (2) the first day the individual was physically present in the U.S. as an LPR.</p> <p>NOTE: See the “Legal Status of Lawful Permanent Residents” Practice Unit.</p>	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(2)(A) ▪ Treas. Reg. § 301.7701(b)-4(a) ▪ DCN:JTO/9431.01_02(2013) 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A


Step 2 (cont'd)

Substantial Presence Test

Step 2: If a year in question is the year of arrival and/or departure, determine the residency start and/or termination date.



DECISION POINT: Did the individual arrive in the U.S. in a year under examination? If so, determine the **residency start** date.

Considerations	Resources	6103 Protected Resources
De minimis rule – An individual may be in the U.S. for up to 10 days without triggering his or her residency start date if the individual is able to establish that, during that period, his or her tax home was in a foreign country and he or she maintained a closer connection to that foreign country than to the U.S. An individual may disregard multiple periods of days so long as the total number of days in all periods does not exceed 10. However, an individual may not disregard any days that occur in a period of consecutive days unless all days in that period can be excluded. Also, any days excluded under this de minimis rule still count for purposes of determining total days of presence. An individual who wishes to exclude days under this rule must file a statement with the IRS.	<ul style="list-style-type: none"> ▪ Treas. Reg. § 301.7701(b)-4(c) 	
 CAUTION: If the individual was a resident alien (under either the SPT or as an LPR) during any part of the preceding calendar year, he or she will be taxable as a resident alien at the beginning of the year under examination.	<ul style="list-style-type: none"> ▪ Treas. Reg. § 301.7701(b)-4(e)(1) 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A


Step 2 (cont'd)

Substantial Presence Test

Step 2: If a year in question is the year of arrival and/or departure, determine the residency start and/or termination date.



DECISION POINT: Did the individual depart from the U.S. in a year in question? If so, determine the **residency termination date**.

Considerations	Resources	6103 Protected Resources
<p>The residency termination date for a person meeting only the SPT is the last day during the year that the individual was physically present in the U.S. if, for the remainder of the calendar year, (1) his or her tax home was in a foreign country <u>and</u> (2) he or she maintained a closer connection to that foreign country than to the U.S.</p> <p>The residency termination date for a person who satisfies the SPT and also was an LPR for the year in question will be <u>the later of</u></p> <ul style="list-style-type: none"> ▪ the first day he or she is no longer and LPR, <u>or</u> ▪ the last day of physical presence in the U.S. <p>if, for the remainder of the calendar year, (1) his or her tax home was in a foreign country <u>and</u> (2) he or she maintained a closer connection to that foreign country than to the U.S.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. § 301.7701(b)-4(b)(2) 	
<p> CAUTION: If the individual was a resident alien (met the SPT or was an LPR) for any part of the year under examination <u>and</u> was a resident alien during any part of the following year (regardless of whether there was a closer connection to a foreign country than to the U.S. in the year under examination), the individual will be taxable as a resident alien through the end of the year under examination.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. § 301.7701(b)-4(e)(2) 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Step 3

Substantial Presence Test

Step 3: Determine whether the individual has filed the appropriate tax return(s).




DECISION POINT: A person who meets the SPT and does not qualify under the closer connection exception must generally file a Form 1040 reporting worldwide income. Under the circumstances below, however, a person meeting the SPT may file a Form 1040NR in addition to, or in lieu of, a Form 1040.

Considerations	Resources	6103 Protected Resources
An individual may be a resident alien for part of a tax year and a nonresident alien for another part of the same year. This issue usually arises in the first or last year of U.S. residency. It may be necessary for such an individual to file <u>both</u> Forms 1040 and 1040NR for the same year.	<ul style="list-style-type: none"> ▪ IRC §§ 7701(b)(3) ▪ Treas. Reg. § 301.7701(b)-4 ▪ Treas. Reg. § 1.6012-1(b)(2)(ii) ▪ Form 1040 ▪ Form 1040NR 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Other Considerations / Impact to Audit

Substantial Presence Test		
Considerations	Resources	6103 Protected Resources
 <p>CAUTION: If a person</p> <ul style="list-style-type: none"> ▪ was treated as a resident alien of the U.S. for at least 183 days in any period which includes at least three consecutive calendar years (initial residency period), ▪ then was treated as a nonresident alien <u>and</u> ▪ subsequently became a resident of the U.S. before the end of the third calendar year beginning after the close of the initial residency period, that person is subject to U.S. income tax in the manner provided by IRC § 877 (expatriation to avoid tax) for the intervening period of nonresident status if the tax exceeds the amount of tax that would be imposed under IRC § 871, relating to the taxation of nonresident aliens. 	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(10) ▪ Treas. Reg. § 301.7701(b)-5 ▪ IRC § 871 ▪ IRC § 877 	

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Glossary of Terms and Acronyms

Acronym	Definition
DCN	Document Control Number
IPN	Issue Practice Network
IPS	Issue Practice Service
LPR	Lawful Permanent Resident
SPT	Substantial Presence Test
UIL	Uniform Issue List

Volume	Part	Chapter	Sub Chapter
Jurisdiction to Tax Outbound	Determination of Residency Status	Substantial Presence Test	N/A

Index of Related Issues

Issue	Associated UIL(s)	References
Election to Treat Nonresident Alien Spouse as Resident Alien		DCN: JTO/9431.02_ xx(201x)
First Year Election		DCN: JTO/9431.02_ xx(201x)
Residency Status of Lawful Permanent Residents		DCN: JTO:/9431.01_02(2013)
Treaties		DCN: TRE/9450.05_ xx(201x)
U.S. Citizens and Residents Failing to File a U.S. Income Tax Return		DCN: JTO/9431.02_04(2013)