

LB&I International Practice Service Process Unit – Audit

Shelf		Individual Outbound		
Volume	9	Jurisdiction to Tax	UIL Code	9431
Part	9.2	Taxation Based on Residency Status	Level 2 UIL	9431.02
Chapter	9.2.5	First Year Election (IRC 7701(b)(4))	Level 3 UIL	9431.02-05
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Unit Name	First-Year Election Under IRC § 7701(b)(4)
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Process Overview

First-Year Election Under IRC § 7701(b)(4)

Process Description

In general, the First-Year Election is used by nonresident alien individuals who arrive in the U.S. after the midway-point of the tax year and do not obtain a green card in that year but do qualify as a resident alien in the following year under the Substantial Presence Test (SPT). Because these individuals do not meet either the SPT or the Green Card Test, they ordinarily are not considered U.S. resident aliens for the tax year in which they arrive. By making the First-Year Election, however, these individuals may be considered U.S. resident aliens for at least part of the tax year, as opposed to being considered a nonresident alien for the entire taxable year.

The purpose of this unit is to determine whether an individual has met the requirements for, and properly made, an election under IRC § 7701(b)(4), commonly referred to as the “First-Year Election”.



CAUTION: This election generally precludes individuals from claiming any U.S. tax benefits under an income tax treaty with respect to the portion of the year they are considered a U.S. resident.

It is important to note that this is an election that individuals must make of their own accord, and not an election that Internal Revenue Service can compel them to make.

Example Circumstances Under Which Process Applies

- An examiner receives a case involving an individual who makes the First-Year election to be treated as a U.S. resident alien for at least part of the tax year in which he arrived in the U.S. The examiner must determine whether the individual meets the requirements for the election, properly made the election and the tax consequences of making the election.

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Determination of Process Applicability

First-Year Election Under IRC § 7701(b)(4)

An individual who makes the First-Year Election is treated as a nonresident alien for part of the tax year and a resident alien for the other part of the tax year.

Criteria	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ In order to make the First-Year Election, the individual generally must satisfy five requirements: <ul style="list-style-type: none"> – Must have been a nonresident alien in the prior year, – Must not meet the SPT or Green Card Test in the current year, – Must satisfy the 31-Consecutive-Day requirement, – Must satisfy the Period of Continuous Presence requirement, and – Must meet the SPT in the subsequent year. 	<ul style="list-style-type: none"> ▪ Form 1040 and/or Form 1040NR ▪ IRC §§ 7701(b)(4)(A)(i)-(iv) ▪ Treas. Reg. §§ 301.7701(b)-4(c)(3)(i)-(iv) 	
<p>NOTE: If the individual is a nonresident alien who is married to a U.S. citizen or resident alien at the end of the tax year, the individual may elect to be treated as a resident alien for the entire tax year under IRC § 6013(g). Similarly, if the individual is a nonresident alien who becomes a U.S. resident during the tax year and is married to a U.S. citizen or resident alien at the end of the tax year, the individual may elect to be treated as a resident alien for the entire tax year under IRC § 6013(h). The election under either IRC § 6013(g) or (h) must be made by both spouses.</p> <p>See the “Election Under IRC § 6013(g)” and “Election Under IRC § 6013 (h)” Practice Units.</p>	<ul style="list-style-type: none"> ▪ IRC §§ 6013(g) and (h) ▪ Treas. Reg. § 1.6013-6 and § 1.6013-7 	

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Summary of Process Steps

First-Year Election Under IRC § 7701(b)(4)	
Step 1	Determine whether the individual met the requirements to make the First-Year Election.
Step 2	Determine whether the individual made a proper First-Year Election.
Step 3	Determine the tax consequences of making the First-Year Election.

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Step 1

First-Year Election Under IRC § 7701(b)(4)

Step 1: Determine whether the individual met the requirements to make the First-Year Election.



DECISION POINT: Did the individual meet all five criteria for making the First-Year Election?

Considerations	Resources	6103 Protected Resources
In order to be eligible to make the First-Year Election, there are five requirements that an individual must meet.	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(4) 	
<p>1. Prior Year: Must be a Nonresident Alien in the Year Prior to the Election Year</p> <ul style="list-style-type: none"> ▪ Individuals wishing to make the First-Year Election must be considered nonresident aliens for U.S. tax purposes in the year before they wish to make the election. This means that such individuals must not have met the Green Card Test or the SPT and must not have made the First-Year Election for the year before the election year. 	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(4)(A)(ii) ▪ Treas. Reg. § 301.7701(b)-4(c)(3)(i)(A) 	
<p>2. Current Year: Must be a Nonresident Alien in the Current Year</p> <ul style="list-style-type: none"> ▪ Individuals wishing to make the First-Year Election must be considered nonresident aliens for U.S. tax purposes in the year of the election as well, which means that such individuals do not meet the Green Card Test or the SPT in the election year (current year). 	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(4)(A)(i) ▪ Treas. Reg. § 301.7701(b)-4(c)(3)(i) 	

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Step 1 (cont'd)

First-Year Election Under IRC § 7701(b)(4)

Step 1: Determine whether the individual met the requirements to make the First-Year Election.



DECISION POINT: Did the individual meet all five criteria for making the First-Year Election?

Considerations	Resources	6103 Protected Resources
<p>3. Current Year: Satisfy the 31-Consecutive-Day Requirement</p> <ul style="list-style-type: none"> ▪ Individuals wishing to make the First-Year Election must be in the United States for 31 consecutive days in the election year, meaning they must be physically present in the U.S during each day of that 31-day period. 	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(4)(A)(iv)(I) ▪ Treas. Reg. § 301.7701(b)-4(c)(3)(iii) and (iv) 	
<p> CAUTION: There are situations that can prevent an individual from counting his or her presence in the U.S. towards this 31-Consecutive-Day requirement. These situations include:</p> <ul style="list-style-type: none"> ▪ If an individual is an exempt individual (i.e., a foreign government-related individual, teacher or trainee, a student, or professional athlete temporarily present in the U.S. to compete in a charitable sports event), ▪ If an individual is present in the U.S. only because he or she has a medical condition which arose in the U.S. and he or she cannot leave because of that medical condition, ▪ If an individual is in the U.S. only because he or she is in the midst of travelling to another foreign country from another foreign country, as transit days are not allowed to be counted, or ▪ If an individual is a regular commuter from Mexico or Canada to the U.S. and he or she commutes to the U.S. for employment purposes. 	<ul style="list-style-type: none"> ▪ Treas. Reg. § 301.7701(b)-3 	

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Step 1 (cont'd)

First-Year Election Under IRC § 7701(b)(4)

Step 1: Determine whether the individual met the requirements to make the First-Year Election.

 **DECISION POINT:** Did the individual meet all five criteria for making the First-Year Election?

Considerations	Resources	6103 Protected Resources
<p>4. Current Year: Satisfy the Period of Continuous Presence</p> <ul style="list-style-type: none"> An individual wishing to make the First-Year Election must also be physically present in the U.S. at least 75% of the days in the current year beginning with (and including) his or her first day of the period that satisfies the 31-Consecutive-Day requirement. This requirement is known as the Period of Continuous Presence requirement. NOTE: In determining whether an individual was in the U.S. for at least 75% of the time for the remainder of the calendar year, the individual in question can count up to 5 days abroad as if he or she was actually present in the U.S. 	<ul style="list-style-type: none"> IRC § 7701(b)(4)(A)(iv)(II) Treas. Reg. § 301.7701(b)-3 Treas. Reg. § 301.7701(b)-4(c)(3)(iv) 	
<p> CAUTION: It is important to remember that the above exception does not apply to the 31-Consecutive-Day requirement where individuals must be physically present in the U.S. each day during that time period.</p>		
<p> CAUTION: There are also some days that an individual could be physically present in the U.S., but those days of presence are not counted towards the period of continuous presence requirement. These instances are the same as those described with respect to the 31-Consecutive-Day requirement.</p>		

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Step 1 (cont'd)

First-Year Election Under IRC § 7701(b)(4)

Step 1: Determine whether the individual met the requirements to make the First-Year Election.



DECISION POINT: Did the individual meet all five criteria for making the First-Year Election? If not, determine whether an exception applies.

Considerations	Resources	6103 Protected Resources
<p>5. Subsequent Year: Satisfy the Substantial Presence Test</p> <ul style="list-style-type: none"> ▪ In the subsequent tax year (the year after the election year), the individual must be physically present in the U.S. for a sufficient number of days in order to satisfy the Substantial Presence test. ▪ Whether an individual obtained a green card in this subsequent year (and therefore would be a resident under the Green Card test) is not relevant for purposes of this requirement. The individual must satisfy the Substantial Presence Test in the subsequent year. 	<ul style="list-style-type: none"> ▪ IRC § 7701(b)(4)(A)(iii) and § 7701(b)(3) ▪ Treas. Reg. § 301.7701(b)-4(c)(3)(i)(B) 	

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Step 2

First-Year Election Under IRC § 7701(b)(4)

Step 2: Determine whether the individual made a proper First-Year Election.



DECISION POINT: Did the individual make a proper First-Year Election?

Considerations	Resources	6103 Protected Resources
<p>When and How to Make the Election:</p> <ul style="list-style-type: none"> Individuals making the First-Year Election to be treated as dual-status aliens do not actually qualify for this election until the SPT is met in the following year. Therefore, an individual who wishes to make this election may request an extension to file his or her tax return in order to allow time to satisfy the SPT. Once the individual has met the SPT, the individual may file a Form 1040 and include a statement indicating they are making the election under IRC § 7701(b)(4). Individuals who make this election can also make an election on behalf of their dependent children so long as (1) the individual making the election qualifies on his or her own behalf, (2) the child qualifies for the election and (3) the child does not have an income tax filing requirement for the election year. 	<ul style="list-style-type: none"> Form 1040 Form 4868 (Automatic Extension of Time to File) Treas. Reg. § 301.7701(b)-4(c)(3)(v)(A) Treas. Reg. § 301.7701(b)-4(c)(3)(v)(B) 	
<p>CAUTION: Individuals making the First-Year Election must still pay any tax owed by the original due date of the return. This payment is also computed as if the individual was a nonresident for the entire election year.</p>		

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Step 2 (cont'd)

First-Year Election Under IRC § 7701(b)(4)

Step 2: Determine whether the individual made a proper First-Year Election.

 **DECISION POINT:** Did the individual make a proper First-Year Election?

Considerations	Resources	6103 Protected Resources
<p>Failure to Comply:</p> <ul style="list-style-type: none"> ▪ If an individual fails to comply with the proper election procedures, such individual then must generally file his or her income tax return as a nonresident alien for the entire tax year, unless the individual can show by clear and convincing evidence that he or she took reasonable actions to become aware of the filing requirements and took significant administrative steps to comply with those requirements. An individual who requests an extension of time to file his or her Form 1040 will be considered to have taken significant administrative steps to comply with the requirement that the individual pay his or her tax determined as if the individual was a nonresident alien if the individual paid with the extension application at least 90 percent of that tax amount. 	<ul style="list-style-type: none"> ▪ Form 1040NR ▪ Treas. Reg. § 301.7701(b)-4(c)(3)(vi) 	

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Step 3

First-Year Election Under IRC § 7701(b)(4)

Step 3: Determine the tax consequences of making the First-Year election.

If a proper First-Year Election is made, an individual will be treated as a U.S. resident for part of the tax year and a nonresident alien for the other part of the tax year. The election cannot be revoked without the consent of the IRS.

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ The individual generally will have filed both Forms 1040 and 1040NR for the election year. The Form 1040 reflects the portion of the year during which the individual was treated as a U.S. resident alien, and the Form 1040NR reflect the portion of the year that the individual was considered a nonresident alien. This dual-status filing requirement usually arises in the first year of U.S. residency, but may also arise in the final year of U.S. residency. ▪ If an individual fails to comply with the proper First-Year Election procedures, then he or she must generally file his or her income tax return as a nonresident alien for the entire tax year ▪ Generally, the individual's residency starting date is the first day of the first period that satisfies the 31-Consecutive-Day requirement, provided the individual also meets the Period of Continuous Presence requirement starting with that same day. 	<ul style="list-style-type: none"> ▪ Form 1040 and/or Form 1040NR ▪ IRC § 7701(b)(4)(C) ▪ Treas. Reg. § 301.7701(b)-4(c)(2) ▪ Treas. Reg. § 1.6012-1(b)(2)(ii) ▪ Form 1040NR ▪ Treas. Reg. § 301.7701(b)-4(c)(3)(vi) ▪ Treas. Reg. § 301.7701(b)-4(c)(3)(iv) 	

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Other Considerations / Impact to Audit

First-Year Election Under IRC § 7701(b)(4)		
Considerations	Resources	6103 Protected Resources
<p>NOTE: If an individual is present for more than one period that satisfies the 31-Consecutive-Day requirement and satisfies the Period of Continuous Presence requirement with respect to each 31-day period, then the earliest of the 31-day periods is used as the residency starting date. However, if the Period of Continuous Presence requirement isn't satisfied with respect to the earliest-31 day period, the individual's residency starting date will begin with the next earliest 31-day period that satisfies the Period of Continuous Presence requirement.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. § 301.7701(b)-4(c)(3)(iv) 	

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Training and Additional Resources

Chapter 9.2.5 First Year Election Under IRC § 7701(b)(4)

Type of Resource	Description(s) and/or Instructions for Accessing	References
Other Training Materials	<ul style="list-style-type: none"> ▪ IRS Publication 519 	

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Glossary of Terms and Acronyms

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

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Index of Related Issues

Issue	Associated UIL(s)	References
Joint Return Election IRC § 6013(g)		▪ DCN: JTO/9431.02_09(2014)
Joint Return Election IRC § 6013(h)		▪ DCN: JTO/9431.02_10(2014)
Residency Status of Lawful Permanent Residents		▪ DCN: JTO/9431.01_02(2013)
Substantial Presence Test		▪ DCN: JTO/9431.01_03(2013)
U.S. Persons Residing Abroad Claiming Additional Child Tax Credit	▪ 9431.06	▪ JTO/9431.06_01(2013)
Tax Home for Purposes of IRC § 911	▪ 9431.06	▪ JTO/CU/P_9.6_05(2013)