# Foreign Earned Income for Purposes of IRC 911

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<td>Primary UIL Code</td>
<td>9431.02-06 Foreign Earned Income Exclusion (IRC 911) - Foreign Earned Income</td>
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<th>INT-C-219</th>
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<td>Date of Last Update</td>
<td>07/27/2020</td>
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Foreign Earned Income for Purposes of IRC 911

The United States taxes its citizens and resident aliens on their worldwide income regardless of where they live or work. Qualifying individuals may be eligible to reduce their U.S. taxable income by claiming the foreign earned income exclusion, the foreign housing exclusion, and/or the foreign housing deduction. These benefits apply to income earned for personal services performed in a foreign country or countries, and are claimed on IRS Form 2555. If the foreign earned income is excluded, an individual cannot also deduct, exclude, or claim a credit (such as the foreign tax credit) or any item that can be allocated to or charged against the excluded amounts.

In order to claim the foreign earned income exclusion, the foreign housing exclusion or the foreign housing deduction, the taxpayer must:

- Have foreign earned income,
- Have a tax home in a foreign country,
- Either be a bona fide resident of a foreign country or physically present in a foreign country or countries for 330 days, and
- Make a valid election.

This unit focuses on the definition of foreign earned income for purposes of Internal Revenue Code (IRC) section 911. The other requirements are discussed in detail in other Practice Units, which are listed on the “Index of Related Practice Units” slide.
### Foreign Earned Income for Purposes of IRC 911

Foreign earned income is income received for services performed in a foreign country during a period in which an individual qualifies for the foreign earned income exclusion.

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<td>The definition of foreign earned income for purposes of Section 911 is found in Internal Revenue Code (IRC) section 911(b)(1). Only income that is attributable to services performed by an individual in a foreign country (or countries) is considered foreign earned income.</td>
<td>IRC 911(b)(1)</td>
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<td></td>
<td>Treas. Reg. 1.911-3(a)</td>
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<td>Treas. Reg. 1.911-2(g)</td>
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<td>Treas. Reg. 1.911-2(h)</td>
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<td></td>
<td>Pub. 54 - Tax Guide for U.S. Citizens and Resident Aliens Abroad</td>
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<tr>
<td><strong>CAUTION</strong>: Not all overseas locations are “foreign countries” – for example, Antarctica, U.S. territories and insular areas, and certain other locations such as international waters and the air space above them.</td>
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<tr>
<td>What Is Foreign Earned Income for Purposes of IRC 911?</td>
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<tr>
<td>- Salaries, professional fees and other compensation received for personal services performed in a foreign country or countries (including noncash income and allowances or reimbursements).</td>
<td>Treas. Reg. 1.911-3(b)(1)</td>
</tr>
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<td>- Any portion of a scholarship or fellowship grant that is paid for teaching, research, or other services performed in a foreign country or countries, if it is included in gross income.</td>
<td>Rev. Rul. 58-222</td>
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<td>- Income from the sale of artistic works or pieces that are the result of the individual's personal efforts performed in a foreign country or countries.</td>
<td>Rev. Rul. 79-85</td>
</tr>
<tr>
<td>- That portion of royalties received by a writer for the transfer of property rights in the writer’s product or under a contract to write a book or series of articles that is allocable to services performed in a foreign country or countries.</td>
<td>Tobey v. Commissioner - 60 T.C. 227 (1973)</td>
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<tr>
<td>Proceeds received in connection with a wage discrimination suit for services performed in a foreign country or countries, as they are restitution for unpaid wages.</td>
<td>▪ Johnson V. Commissioner - T.C. Memo 1977-377</td>
</tr>
<tr>
<td>In the case of an individual engaged in a trade or business (other than in corporate form) where capital investment is an important part of producing income, a reasonable allowance as compensation for personal services actually performed by the individual in a foreign country (or countries) is considered foreign earned income.</td>
<td>▪ Treas. Reg. 1.911-3(b)(2)</td>
</tr>
<tr>
<td>CAUTION: If capital investment is an important part of producing income, no more than 30% of the individual's share of net profit from the business, after the deduction on Form 1040 for one-half of self-employment tax, is considered earned income. Of that, only the portion that represents compensation for personal services performed in a foreign country or countries is considered foreign earned income.</td>
<td>▪ IRC 911(d)(2)(B)</td>
</tr>
<tr>
<td>Generally, rental income is unearned income. However if personal services are performed in connection with the production of rent, up to 30% of the net rental income can be considered earned income. For example, J, a U.S. citizen living in England, owns and operates a rooming house in London. If he is operating the rooming house as a business that requires capital and personal services, he can consider up to 30% of net rental income as earned income. On the other hand, if he just owns the rooming house and performs no personal services connected with its operation, except perhaps making minor repairs and collecting rents, none of his net income from the house is considered earned income. It is all unearned income.</td>
<td>▪ Pub. 54 - Tax Guide for U.S. Citizens and Resident Aliens Abroad</td>
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<td>Severance payments received by a terminated employee may be earned income when the payment is in the nature of compensation for past services and does not represent consideration for cancellation of an employment contract or in respect of a noncompete agreement. If that is the case, then only the portion of the severance payment that is allocable to services performed in a foreign country or countries is foreign earned income.</td>
<td>• Rev. Rul. 79-6</td>
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| Stock options may be earned income if the stock disposed of was stock received by exercise of a stock option granted under an employee stock purchase plan. If the gain on the disposition of stock by exercise of an option is treated as capital gain, the gain is unearned income. However, if the stock was disposed of in less than two years after the option was granted or less than one year after the stock was received, part of the gain on the disposition may be earned income. It is considered received in the year the stock was disposed of and earned in the year services were performed for which the option was granted. Only the portion that is due to services performed in a foreign country or countries is foreign earned income. | • Rev. Rul. 69-118  
• Groetzinger v. Commissioner - 87 T.C. 533 (1986) |
| That portion of amounts received as sick leave pay or vacation pay are considered foreign earned income to the degree they are allocable to services performed in a foreign country or countries. | • Chidester v. U.S. - 82 F. Supp. 322 (Ct. Cl.1949) |
| Commissions received by a retired individual upon the renewal of insurance policies that previously solicited by that individual represent compensation for personal services, even though the individual has retired and no longer services the policyholders. The portion of such commissions that is allocable to services performed in a foreign country or countries is foreign earned income. | • Rev. Rul. 63-99 |
### Detailed Explanation of the Concept (cont’d)

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<td>• PLR 8619051</td>
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<tr>
<td>• Research fellowships from private foundations may constitute foreign earned income where the fellowship stipend is designed to replace lost salary allocable to services performed in a foreign country or countries.</td>
<td>• <em>Miller v. Commissioner</em> - 52 T.C. 752 (1969)</td>
</tr>
<tr>
<td>• A guaranteed payment received by a partner is considered foreign earned income if it was paid for services performed in a foreign country, regardless of whether the partnership has any profits.</td>
<td>• IRC 704(a)</td>
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<td>– The income is determined at the partnership level. Once the partnership's foreign earned income is determined, it is allocated among the partners based on the partnership agreement. This agreement must have substantial economic effect.</td>
<td>• IRC 704(b)</td>
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<tr>
<td>• The fair market value of fringe benefits, including the right to use an employer's property or facilities, is earned income.</td>
<td>• IRC 707(c)</td>
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<td>What Is NOT Foreign Earned Income for Purposes of IRC 911?</td>
<td>• Rev. Rul. 67-158</td>
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<td>• Dividends, interest, capital gains and alimony.</td>
<td>• Treas. Reg. 1.704-1</td>
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<td>• Pension or annuity (included social security benefits).</td>
<td>• Rev. Rul. 81-300</td>
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<td>• Compensation paid to an employee by an employer which is the U.S. government or any of its agencies or instrumentalities.</td>
<td>• Rev. Rul. 81-301</td>
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<td>• Pub. 54 - <em>Tax Guide for U.S. Citizens and Resident Aliens Abroad</em></td>
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<td>• Any amount included in the individual's gross income due to the taxability of a nonexempt trust or the taxability of a beneficiary under a nonqualified annuity or annuities purchased by exempt organizations.</td>
<td>Treas. Reg. 1.911-3(c)(4)</td>
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<td>• Income from gambling activities.</td>
<td>IRC 402(b)</td>
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<td>• Any portion of an amount paid by a corporation which represents a distribution of earnings and profits rather than a reasonable allowance as compensation for personal services actually rendered to the corporation.</td>
<td>IRC 403(c)</td>
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<td>• Income excluded from gross income as meals and lodging provided by an employer under IRC 119.</td>
<td>Rev. Rul. 55-171</td>
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<td>• Employee expenses reimbursed under an accountable plan for expenses incurred on the employer’s behalf which have adequately been accounted for to the employer.</td>
<td>Treas. Reg. 1.911-3(b)(1)</td>
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<tr>
<td>• Any amount received after the close of the first taxable year following the taxable year in which the services giving rise to that amount were performed.</td>
<td>Treas. Reg. 1.911-3(c)(1)</td>
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<td>• Royalties from the leasing of oil and mineral rights or patents.</td>
<td>Pub. 54 - <em>Tax Guide for U.S. Citizens and Resident Aliens Abroad</em></td>
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<td>• IRS.gov - <em>Foreign Earned Income Exclusion - What is Foreign Earned Income</em></td>
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<td>• IRS.gov - <em>Foreign Earned Income Exclusion</em></td>
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