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IRS Provides Limited Relief to Cross-Border Taxpayers Stranded by COVID-19

The IRS issued three pieces of guidance last week—two revenue procedures and an FAQ—to provide relief to taxpayers whose inability to travel internationally during the COVID-19 pandemic would otherwise affect their federal income tax status or liability:

- Revenue Procedure 2020-20 offers limited relief (up to 60 days) to non-U.S. individuals stuck in the United States who would otherwise become U.S. residents under the normal day counting rules.
- Revenue Procedure 2020-27 enables otherwise eligible U.S. citizens and residents who were working abroad, but who had to cut their trips short on account of COVID-19, to continue to qualify for the foreign earned income exclusion.
- The FAQ provides a 60-day safe harbor for activities conducted on behalf of a foreign corporation or nonresident alien which otherwise could cause a nonresident alien or foreign corporation for which they were performed to be considered to be engaged in a U.S. trade or business for tax purposes.

Because relief from the day counting rules is capped at 60 days, its efficacy will depend on how long travel disruptions continue. Further, while foreign companies will no doubt welcome a partial safe harbor from being pulled into the federal corporate tax net, they could still face corporate tax exposure in some states and localities, not to mention wage withholding, payroll tax, unemployment insurance and workers compensation requirements.

An eligible individual may claim the COVID-19 travel exception in addition to, or instead of, claiming other exceptions from the substantial presence test. All other applicable exceptions are available, but Revenue Procedure 2020-20 notes, in particular, that an individual who would be a U.S. resident even after excluding eligible days under the COVID-19 travel exception may still exclude days outside the COVID-19 emergency period on the basis of an actual medical condition that arises unexpectedly while visiting the United States. Relief also may be sought under the closer connection test, as well as under applicable treaty "tie-breaker" provisions.

Revenue Procedure 2020-20: Exclusion of Days from Day Count

Revenue Procedure 2020-20 addresses the classification of noncitizens as U.S. residents for federal income tax purposes under the "substantial presence test" of Section 7701(b)(3) of the Internal Revenue Code (the Code).

U.S. citizens and residents are taxable in the United States on their worldwide income. In general, noncitizens are considered U.S. residents for federal income tax purposes if either (a) they are lawful permanent residents (green card holders) or (b) meet the "substantial presence test." An individual meets the substantial presence test if such individual (1) is physically present in the United States for at least 31 days during the current calendar year and (2) has a weighted day count of 183 days or more. An individual's weighted day count is the sum of (i) his or her days present in the United States during the current calendar year, (ii) one-third of his or her days present during the immediately preceding calendar year and (iii) one-sixth of his or her days present during the second preceding calendar year. In general, someone who spends more than 121 days in the United States per year is likely to become a resident under this test.

There are a number of exceptions to the normal day counting rules, including for individuals who can establish that they have a closer connection to another country and a tax home therein, individuals present on certain visas, and individuals who are

unable to leave the United States on account of an unexpected medical emergency that arises while visiting the United States. It is this last exception that provides the basis for COVID-19 relief.

Under Revenue Procedure 2020-20, in applying the substantial presence test, an "Eligible Individual" who intended to leave the United States but was unable to as a result of travel disruptions (including canceled flights, shelter-in-place orders, quarantine and closed borders), or because he or she felt that traveling would be unsafe due to recommendations to implement social distancing and limit exposure to public spaces, may exclude a period of up to 60 consecutive days of presence in the United States beginning on or after February 1, 2020, and on or before April 1, 2020 (the COVID-19 Emergency Period). An Eligible Individual is any individual who was not a resident at the close of the 2019 tax year, is not a lawful permanent resident at any point during 2020, is present during each of the days of his or her COVID-19 Emergency Period, and does not otherwise become a resident due to his or her days of presence in the United States outside of the COVID-19 Emergency Period. Eligible Individuals are presumed to have intended to leave the United States during their COVID-19 Emergency Period unless they have applied or otherwise taken steps to become lawful permanent residents of the United States.

Eligible Individuals who are required to file Form 1040-NR for 2020 must claim this exception by attaching Form 8843 to their timely filed 2020 returns, completed as specified in the revenue procedure. Eligible individuals who are not otherwise required to file Form 1040-NR for 2020 do not have to file a Form 8843 to claim this exception but are encouraged to retain all relevant records and be prepared to file a Form 8843 if one is requested by the IRS in the future.

Revenue Procedure 2020-27

Revenue Procedure 2020-27 addresses the eligibility of certain U.S. citizens living abroad to exclude foreign earned income from U.S. income taxation.

Section 911(a) of the Code allows "qualified individuals" to elect to exclude foreign earned income and certain housing costs from gross income. A qualified individual is an individual whose tax home is in a foreign country and who is either (a) a U.S. citizen who has been a bona fide resident of a foreign country for an uninterrupted period that includes the entire taxable year or (b) a U.S. citizen or resident who is present in a foreign country or countries for at least 330 full days during any period of 12 consecutive months. Additionally, Section 911(d)(4) provides that individuals may be treated as qualified individuals if the Secretary of the Treasury determines that they were required to leave the foreign country in which they were resident because of war, civil unrest or similar adverse conditions.

Under Revenue Procedure 2020-27, the COVID-19 pandemic has been deemed an adverse condition precluding the normal conduct of business in most of China (excluding Hong Kong and Macau) from December 1, 2019, through July 15, 2020, and globally from February 1, 2020, through July 15, 2020. Therefore, individuals who left China on or after December 1, 2019, or any other country on or after February 1, 2020, but before July 15, 2020, will be treated as qualified individuals if they otherwise would have met the requirements to be qualified individuals but for the COVID-19 pandemic. To qualify for relief under the revenue procedure, an individual must have established residency or have been physically present in the foreign country on or prior to December 1, 2019, or February 1, 2020, as applicable.

New FAQ: Relief for U.S. Trade or Business Activities

Nonresident alien individuals who perform services or other activities in the United States and foreign corporations that employ individuals or engage individuals as agents to perform services or other activities in the United States may be considered to be engaged in a U.S. trade or business. Generally, a nonresident alien or foreign corporation that is engaged in a U.S. trade or business is taxable on income that is effectively connected with a U.S. trade or business. Further, if a U.S. or foreign partnership is engaged in a U.S. trade or business, then all of its partners (including foreign partners) will be deemed to be so engaged for tax purposes.

If individuals performing such services or other activities are temporarily in the United States solely due to COVID-19 travel disruptions, then nonresident aliens or foreign corporations (or partnerships of which either are members) for which such services are performed may choose an uninterrupted period of up to 60 calendar days beginning on or after February 1, 2020, and on or before April 1, 2020, during which such services or other activities will not be taken into account in

determining whether they are engaged in a U.S. trade or business. The FAQ provides a similar 60-day exclusion for purposes of determining whether a nonresident alien or foreign corporation has a permanent establishment in the United States under an income tax treaty.

The nonresident alien or foreign corporation relying on this exception should retain contemporaneous documentation to establish the period chosen and that the relevant business activities conducted by an individual temporarily present in the United States during this period would not have been undertaken in the United States but for the travel disruptions. Consideration should be given to filing a protective tax return (e.g., to run the statute of limitations and leave the door open to claiming deductions) even if one is not otherwise required.

This relief will be of particular interest to foreign companies that have officers or employees stranded in the United States who need to continue working, as this may help prevent these companies from having their earnings pulled into the United States, at least at the federal level. However, the FAQ does not address potential wage withholding, payroll tax and unemployment insurance obligations, and employers may have to contend with similar issues at the state or local level, although some states have begun introducing their own safe harbors. Thus, it will be important for affected businesses to consult with their tax and employment advisors sooner rather than later.

For more Day Pitney alerts and articles related to the impact of COVID-19, as well as information from other reliable sources, please visit our COVID-19 Resource Center.

COVID-19 DISCLAIMER: As you are aware, as a result of the COVID-19 pandemic, things are changing quickly and the effect, enforceability and interpretation of laws may be affected by future events. The material set forth in this document is not an unequivocal statement of law, but instead represents our best interpretation of where things stand as of the date of first publication. We have not attempted to address the potential impacts of all local, state and federal orders that may have been issued in response to the COVID-19 pandemic.

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