



## International Tax ADVISORY ■

**JUNE 15, 2020**

### Who Says You Can't Go Home? IRS Sends Care Package to Those Away from Home Due to COVID-19

COVID-19 has upended life around the world with many unexpected consequences. Thanks to new IRS guidance, those consequences may not come in the form of an unexpected tax bill for individuals and businesses present in the U.S. for longer than planned during 2020 due to COVID-19.

Travel disruptions due to the COVID-19 pandemic has made it very difficult to conduct business as planned. Some individuals were stranded in the U.S. due to canceled flights or fear of traveling and contracting the virus. Others, who planned to work abroad this year, returned to the U.S. early due to the pandemic. These disruptions created a risk that, without further guidance from the IRS, foreign individuals who did not plan on an extended stay in the U.S. this year would become U.S. tax residents or would lose treaty benefits on income from dependent personal services performed in the U.S., businesses would be considered engaged in a U.S. trade or business or would be deemed to have a U.S. permanent establishment, and U.S. citizens and residents who planned to be resident in a foreign country would lose the foreign earned income exclusion under Internal Revenue Code Section 911. The recent package of guidance issued by the IRS provides relief to these individuals and businesses, provided they meet certain requirements.

#### **Alien Individuals and Revenue Procedure 2020-20**

Generally, an alien individual without a green card who meets the substantial presence test (SPT) in any year will be treated as a U.S. resident for federal tax purposes for that year. The substantial presence test is met for a tested calendar year if (1) an alien individual is physically present in the U.S. for at least 31 days during the tested calendar year; and (2) the sum of the number of days present in the tested calendar year, plus one-third of the number of days present in the preceding calendar year, plus one-sixth of the number of days present in the second preceding year is at least 183 days.

In some circumstances, days physically present in the U.S. can be excluded from the SPT calculation. The medical condition exception allows an alien individual to exclude days present in the U.S. when the individual intended to

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leave the U.S. but was unable to do so because of a medical condition that arose while the individual was present in the U.S. However, no exclusion is allowed if the individual was aware of the medical condition before arriving. A similar medical condition exception exists when determining the availability of treaty benefits for income from dependent personal services performed in the U.S.

Recent IRS guidance issued in [Rev. Proc. 2020-20](#) expands on the medical condition exception and provides a “COVID-19 medical condition travel exception” for “eligible individuals.” An eligible individual is any individual who (1) was not a U.S. resident at the close of the 2019 tax year; (2) is not a lawful permanent resident at any point in 2020; (3) is present in the U.S. on each of the days of the individual’s COVID-19 emergency period; and (4) does not become a U.S. resident in 2020 due to days present in the U.S. outside the individual’s COVID-19 emergency period.

Rev. Proc. 2020-20 allows eligible individuals who intended to leave the U.S. during the individual’s COVID-19 emergency period but were unable to do so due to “COVID-19 emergency travel disruptions” to exclude the COVID-19 emergency period from their SPT calculation. This exclusion is also allowed when determining eligibility for treaty benefits under an applicable U.S. income tax treaty for income from employment or other dependent personal services performed in the U.S. The COVID-19 emergency period is defined as a single period of up to 60 consecutive calendar days selected by the eligible individual starting on or between February 1, 2020 and April 1, 2020.

Despite its name, the COVID-19 medical condition travel exception does not require the individual to contract COVID-19 in the U.S. (this would be covered by the general medical condition exception, which may be claimed instead of, or in addition to, the COVID-19 medical condition travel exception). Instead, COVID-19 emergency travel disruptions include restrictions on the movement of individuals by canceled flights or other disruptions in transportation, stay-at-home orders, quarantines, border closures, and orders of government authorities. Also included are eligible individuals who choose not to travel as planned due to safety concerns based on recommendations to implement social distancing and limit exposure to public spaces.

The definition of COVID-19 emergency travel disruptions is broad and somewhat subjective, and it appears that Rev. Proc. 2020-20 recognizes this. Instead of requiring that an eligible individual prove that the exception’s requirements are met, Rev. Proc. 2020-20 presumes that any eligible individual intended, but was unable, to leave the U.S. on any day during the individual’s COVID-19 emergency period. However, an eligible individual loses this presumption if the individual has applied for a green card or otherwise taken steps to become a U.S. permanent resident.

## **U.S. Citizens Abroad and Revenue Procedure 2020-27**

A U.S. citizen or resident who is a “qualified individual” may elect to exclude foreign earned income and foreign housing costs from gross income for U.S. federal tax purposes (the “foreign earned income exclusion”) under Section 911. A “qualified individual” is either (1) a U.S. citizen whose tax home is in a foreign country and has been a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire taxable year; or (2) a U.S. citizen or resident of the U.S. whose tax home is in a foreign country and who is present in a foreign country or countries for at least 330 full days during any 12 consecutive months.

An individual who fails to meet the definition of “qualified individual” because he or she is required to leave the foreign country due to war, civil unrest, or similar adverse conditions that precluded the normal conduct of business (as determined by the Secretary of the Treasury) may still be eligible for the foreign earned income exclusion under Section 911(d)(4). Such individual will still be treated as a qualified individual if he or she can establish that, but for the adverse conditions, the individual could reasonably have been expected to meet the qualified individual definition.

[Rev. Proc. 2020-27](#) establishes that the COVID-19 pandemic is an adverse condition for purposes of Section 911(d)(4). COVID-19 became an adverse condition in the People's Republic of China, excluding the special administrative regions of Hong Kong and Macau, as of December 1, 2019, and became an adverse condition globally as of February 1, 2020 (each an "applicable date"). The adverse condition period ends globally (including China) on July 15, 2020, unless the IRS announces an extension. To qualify for relief under this Revenue Procedure, an individual must have been physically present or established residency in a foreign country before the applicable date and must have left that foreign country on or after the applicable date. The individual must also establish that there was a reasonable expectation that he or she would meet the definition of qualified individual but for the COVID-19 pandemic.

## Engaged in Trade or Business and the Frequently Asked Questions

In addition to the two Revenue Procedures, the IRS issued a set of frequently asked questions (FAQs) addressing whether a nonresident individual who cannot leave the U.S. due to the COVID-19 pandemic will be considered engaged in a U.S. trade or business (USTB) or if employees of a foreign company will cause the company to be engaged in a USTB.

The FAQs extend the concepts in Rev. Proc. 2020-20 to nonresident aliens, foreign corporations, or a partnership in which a foreign corporation or nonresident alien individual is a partner (each an "affected person") for purposes of determining whether the affected person is engaged in a USTB. An affected person may exclude activities performed in the U.S. during its COVID-19 emergency period (using the same definition as in Rev. Proc. 2020-20) from determining if it is engaged in a USTB provided that (1) the activities were performed by one or more individuals temporarily present in the U.S.; and (2) would not have been performed in the U.S. but for COVID-19 emergency travel disruptions (using the same definition as in Rev. Proc. 2020-20). For purposes of the FAQs, an "individual temporarily present in the United States" includes both nonresident alien individuals (determined by including the guidance in Rev. Proc. 2020-20) and U.S. citizens or permanent residents who had a tax home outside the U.S. in 2019 and reasonably expect to have a tax home outside the U.S. in 2020.

An individual or corporation that is engaged in a USTB is subject to tax in the U.S. on any business income connected to that USTB unless a U.S. income tax treaty applies. If a U.S. income tax treaty applies, income from a USTB is generally not subject to tax unless the USTB is conducted through a permanent establishment in the U.S. (USPE). The FAQs further provide that activities performed by individuals temporarily present in the U.S. during an affected person's COVID-19 emergency period will not be considered when determining if a nonresident or foreign corporation has a USPE, provided that the activities would not have occurred in the U.S. but for the COVID-19 emergency travel disruptions. If an affected person is treated as not having a USTB or USPE solely because of the guidance in the FAQs, the income earned by the affected person during the COVID-19 emergency period will not be subject to the 30% gross basis tax imposed under Section 871(a) or Section 881(a).

The FAQs generally advise that any affected person should retain contemporaneous documentation showing that they meet the requirements for relief as provided by the FAQs. The FAQs also provide that affected persons may make protective filings of their annual U.S. tax returns, even if they believe they are not engaged in a USTB under the guidance in the FAQs. A protective filing allows a taxpayer to avail themselves of the benefits and protections of filing a return, including beginning the clock on the statute of limitations.

## Reliability of Guidance

A revenue procedure is an official IRS statement of a procedure that affects the rights or duties of taxpayers under the Code, Treasury regulations, tax treaties, and related statutes that should be a matter of public knowledge. As the IRS's

official published position, revenue procedures can always be relied on by the public. This is not the case for FAQs published on the IRS website. FAQs are unofficial IRS guidance that can be changed or removed at any time, and the IRS takes the position that FAQs cannot be relied on despite being published by the IRS itself.

Since FAQs cannot generally be relied on, taxpayers who hope to avoid being engaged in USTB by meeting the requirements set out in the FAQs should exercise caution. Extensive documentation supporting the taxpayer's position is recommended, and a protective filing to begin the running of the statute of limitations on the 2020 year is advisable.

For more information, please contact [Edward Tanenbaum](#) at 212.210.9425 or [April McLeod](#) at 212.210.9487

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