

Taxes Are Due on Arrival in the United States

# Exploring the Unique Tax Complexities Faced by Foreign Professionals Coming into the U.S.

By Andrew Fisher, CFA, CPA

## Overview

More than ever, foreign professionals are coming into the United States to work, and generally we all benefit. However, incoming workers need to understand the numerous potential tax traps they face.

Foreign citizens moving into the United States are an increasing population due to the ongoing globalization of business. They tend to be accomplished professionals who save at a much higher rate than their American peers. However, they also have far more complicated financial affairs than a typical American, and both their financial planning and investing needs can be quite different. As financial planners and wealth advisors who specialize in cross-border families, many of our clients are foreign nationals living in the United States, who are looking for clarity on their taxes and other financial situations.

This article, then, is a primer on the typical tax issues confronting this group.

Foreign nationals living in the United States are technically referred to as “resident aliens” by the IRS, but they can also be known as “tax residents,” “U.S. residents,” or “permanent residents” (if they hold a green card). It is important to understand that while they are here in the United States, most will generally be taxed the same as any other American, except with the added complexity that they often own assets located outside of the United States and have additional foreign tax responsibilities.

## Learning the U.S. Tax System

Foreign nationals often struggle with understanding the U.S. tax code, with its complexity and worldwide reach. For those who are used to a less complex or “flat” tax system, the U.S. tax code and its requirements can be truly mind-boggling. Similarly, foreign nationals are often faced with making decisions as to various retirement and investment options that are completely unfamiliar.

Many foreign nationals who work for large corporations come to the United States on short-term work visas or temporary assignments, which means they are somewhat insulated from the full ramifications of becoming a U.S. tax resident. They will usually be required to file a U.S. tax return and will be taxed on U.S.-sourced income but often not on any foreign-sourced income, depending on their visa status.

## Becoming a U.S. Resident for Tax Purposes

Foreign citizens who are newly arrived in the United States often misunderstand both whether they will be classified as a tax resident as well as what it means to be so classified. Some will have accumulated assets such as cash, real estate, investment portfolios, and retirement savings accounts overseas. These foreign assets can be immediately subjected to U.S. taxation, which often comes as a big and unwelcome surprise. For that reason, correctly planning

a move to the United States is extremely important.

There are situations in which a visiting worker can remain a nonresident for tax purposes and will only be taxed on his or her U.S.-sourced income. In contrast, U.S. tax residents are taxed on their worldwide income. For example, consider someone who owns a foreign business and comes to the United States for a short time to launch a subsidiary, and then ends up staying here longer than originally planned. This person could end up being classified as a U.S. tax resident, which could potentially expose his or her entire worldwide business operations to U.S. taxation. That would come as quite a nasty surprise to someone who did not realize they had become a U.S. tax resident.

## Two Tests to Determine U.S. Residency

There are two tests used to determine whether a foreign person has become a U.S. tax resident. Anyone who meets the requirements of either of these two tests will be treated as a U.S. tax resident. These two tests are:

1. The lawful permanent resident test
2. The substantial presence test

### LAWFUL PERMANENT RESIDENT TEST (THE “GREEN CARD” TEST)

The first of the two tests for determining whether someone is a U.S. tax resident is very straightforward. A foreign national is considered a U.S. permanent resident if he or she has been issued a green card granting them the privilege of residing permanently in the United States. One important feature of a green card is that it can be surrendered by its holder, and, of course, it can also be revoked by U.S. immigration authorities. The tax status and treatment of a green card holder is, for almost all purposes, exactly the same as that of a U.S. citizen.

### SUBSTANTIAL PRESENCE TEST

The second test, known as the substantial presence test, is more complicated and relies on the number of days someone has been physically present in the United States for the current year plus the two prior years. Being present here for 183 days in the current year means the test has already been met. According to the IRS:<sup>1</sup>

*You will be considered a U.S. resident for tax purposes if you meet the substantial presence test for the calendar year. To meet this test, you must be physically present in the United States on at least:*

- 31 days during the current year, and
- 183 days during the 3-year period that includes the current year and the 2 years immediately before that, counting:
  - » All the days you were present in the current year, and
  - » 1/3 of the days you were present in the first year before the current year, and
  - » 1/6 of the days you were present in the second year before the current year.

There are certain exceptions to the substantial presence test. For example, any days spent in the United States as an exempt person—such as a government official here on business or a traveling teacher, student or athlete—will not count as part of the total number of days. And, according to the formula, if someone spent less than 31 days in the current year, he or she does not meet the test. Another exception is called the “closer connection exception.” Here, even if one meets the substantial presence test according to the above formula, it can be argued that there is a taxable residence maintained in another country with a closer connection to that country. This exception, however, is pretty rare. Finally, if one has remained a tax resident in a home country, it is possible to be able to use an international treaty—if there is one—to avoid being considered a U.S. resident.

Once the residency status is determined, one major complication for foreign citizens is the increased reporting of personal foreign assets to the U.S. government via the Report of Foreign Bank and Financial Accounts (FBAR) on Financial Crimes Enforcement Network (FinCEN) Form 114 as well as Form 8938, Statement of Specified Foreign Financial Assets. Foreign citizens often view these requirements with suspicion and as an invasion of privacy.

## Foreign Citizens Leaving the United States for Short-Term Assignments

Occasionally, foreign citizens who are permanent tax residents of the United States will pursue an opportunity abroad without necessarily planning to stay away from the United States forever. For that reason, many of them do not give up their green card just because they've left. The downside to holding onto their green card, however, is that they continue to be viewed—and taxed—by the IRS in the exact same way that an American citizen is taxed for as long as they retain their permanent tax residency. Of course, this also applies to foreign nationals who have become U.S. citizens or dual citizens.

Cross-border tax laws are inherently complex, and we generally recommend that our clients work with professional tax preparers familiar with cross-border issues. Good advice pays off in the long run.

---

<sup>1</sup> <https://www.irs.gov/individuals/international-taxpayers/substantial-presence-test>

Cerity Partners LLC (“Cerity Partners”) is an SEC-registered investment adviser with office locations throughout the United States. Registration of an Investment Advisor does not imply any level of skill or training. The foregoing is limited to general information about Cerity Partners’ financial market outlook. You should not construe the information contained herein as personalized investment, tax, or legal advice. There is no guarantee that the views and opinions expressed in this commentary will come to pass. The information presented is subject to change without notice and should not be considered as an offer to sell or a solicitation of an offer to buy any security. Material economic conditions and/or events may affect future results. All information is deemed reliable as of the date of this commentary but is not guaranteed. Before making any decision or taking any action that may affect your finances or your company’s finances, you should consult a qualified professional adviser. For information pertaining to the registration status of Cerity Partners, please contact us or refer to the Investment Adviser Public Disclosure website ([www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov)). For additional information about Cerity Partners, including fees, conflicts of interest, and services, send for our disclosure statement as set forth on Form CRS and ADV Part 2 using the contact information herein. Please read the disclosure statement carefully before you invest or send money.

**[ceritypartners.com/contact](http://ceritypartners.com/contact)**