

Residency/presence tests for foreign exclusions waived because of pandemic

In response to the novel coronavirus (COVID-19) pandemic, the IRS has waived the residency and presence tests that apply for purposes of the 2019 and 2020 foreign earned income and foreign housing cost exclusions under Internal Revenue Code Section 911. The waiver generally applies to certain U.S. individuals who were in China as of December 1, 2019, or were otherwise outside the United States as of February 1, 2020.

Defining a qualified individual

Sec. 911(a) allows a “qualified individual” to exclude foreign earned income and foreign housing costs from his or her gross income. Sec. 911(d)(1) defines the term “qualified individual” as someone whose tax home is in a foreign country and who’s:

- A U.S. citizen of and establishes, to the satisfaction of the IRS, that he or she has been a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire tax year, or
- A citizen or resident of the United States who, during any period of 12 consecutive months, is present in a foreign country or countries for at least 330 full days.

Sec. 911(d)(4), however, provides that an individual will be treated as a qualified individual for a period during which the individual was a bona fide resident of, or was present in, a foreign country if he or she left the country during a period for which the U.S. Department of the Treasury, in consultation with the U.S. Department of State, determines that people were forced to leave because of war, civil unrest or similar adverse conditions that precluded the normal conduct of business. An individual must establish that, but for these conditions, he or she could reasonably have been expected to meet the eligibility requirements (referred to below as the “reasonable expectation rule”).

The IRS has previously listed countries for 2019 for which the eligibility requirements of Sec. 911(d)(1) are waived under Sec. 911(d)(4).

Specifying the time period

For 2019 and 2020, and for purposes of Sec. 911(d)(4), the COVID-19 crisis is considered an adverse condition that precluded the normal conduct of business:

- In the People’s Republic of China, excluding the Special Administrative Regions of Hong Kong and Macau (China), as of December 1, 2019, and
- Globally, as of February 1, 2020.

The period covered by this Revenue Procedure ends on July 15, 2020, unless an extension is announced by the Treasury Department and the IRS. Thus, for Sec. 911 purposes, someone who left China on or after December 1, 2019, or another foreign country on or after February 1, 2020 — but on or before July 15, 2020 — will be treated as a qualified individual with respect to the period during which he or she was present in, or was a bona fide resident of, that foreign country. This applies if the person establishes a reasonable expectation that he or she would have met the requirements of Sec. 911(d)(1) but for the COVID-19 crisis.

To qualify for relief under Sec. 911(d)(4), an individual must have established residency, or have been physically present, in the foreign country on or before the applicable date specified above. Therefore, someone who was first physically present or established residency in China after December 1, 2019, or another foreign country after February 1, 2020, would be ineligible.

Anyone seeking to qualify for the Sec. 911 foreign earned income exclusion because he or she could reasonably have been expected to have been present in a foreign country for 330 days but for the COVID-19 pandemic, and who has met the other requirements for qualification, may use any 12-month period to meet the qualified individual requirement.

Considering examples

Say an individual arrived in China on September 1, 2019, and established that he or she reasonably expected to work in China until September 1, 2020. But this person departed China on January 10, 2020, because of the COVID-19 crisis.

He or she would be a qualified individual for the period from September 1, 2019, through December 31, 2019, and for the period from January 1, 2020, through January 9, 2020, because he or she met the Sec. 911(d)(4) reasonable expectation rule (assuming the individual also met the other qualification requirements under Sec. 911).

Or, let's say an individual who was present in the United Kingdom on January 1, 2020, through March 1, 2020, established that he or she reasonably expected to work in the United Kingdom for the entire calendar year. But he or she departed the United Kingdom on March 2, 2020, because of COVID-19, and later returns to the United Kingdom on August 25, 2020, staying for the rest of the calendar year.

He or she would be a qualified individual for 2020 with respect to the period between January 1, 2020, through March 1, 2020, and August 25, 2020, through December 31, 2020, because he or she met the Sec. 911(d)(4) reasonable expectation rule (assuming the individual also met the other qualification requirements under Sec. 911).

Understanding the impact

The IRS notes that previously issued Revenue Procedures under Sec. 911(d)(4) remain in full force and effect. If you believe the waived residency and presence tests may apply to you, work with your CPA to understand the impact on your tax situation. •