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INTERNATIONAL TAX

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Helping Work Globally

A successful multi-national business or investor must consider the tax consequences of business or investment decisions. We can help you comply with tax reporting requirements that have a significant impact on your bottom line.

Global Employment Earnings: Alternative for a Mobile Workforce

Global workforce mobility has become commonplace among large multi-national businesses. As small and mid-size businesses grow and expand overseas, there may be a need to have a trusted employee on the ground abroad to get the expanded business up and running.

Working abroad can be a wonderful, enlightening experience for the employee. Unfortunately, it can also present some income tax complications.

U.S. citizens and permanent residents are taxed on their worldwide income. Generally, countries tax the worldwide income of individuals resident in that country. This means a U.S. citizen or permanent resident who sojourns in another country for more than a brief period may be subject to tax in both places. As you might imagine, for a mobile workforce, this can be problematic. Fortunately, the Foreign Earned Income Exclusion (FEIE) and the Foreign Housing Exclusion (FHE) are available to help mitigate double taxation

Generally, the FEIE excludes employment income earned abroad (subject to a limitation) from U.S. taxable income.

The FHE allows a qualified individual to make a separate election to exclude the cost of housing provided by the employer from his or her gross income. The basic concept of this additional exclusion is to give individuals a tax break for housing expenses incurred overseas that exceed average housing costs in the United States.

Residence Tests

There are two tests to qualify for the exclusions: the bona fide residence test and the physical residence test.

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Bona Fide Residence Test. In order for a taxpayer to qualify for this test, the taxpayer must show that he or she was a bona fide resident of the foreign country for an uninterrupted period that includes an entire taxable year.

The bona fide residence test is substantive, meaning it is a "facts and circumstance" test that sets to prove whether the taxpayer is considered a resident of a foreign country based on a number of factors. Such factors include, among many others, the taxpayer's intention to reside in the country; establishment of a home in the foreign country; nature, extent and reasons for temporary absences from the foreign home; etc.

Physical Presence Test. This test requires the taxpayer to be present within the foreign country for at least 330 full days during any consecutive 12-month period. For this purpose, the definition of a full day is a 24-hour period. If the person leaves the country for any length of time on any day, then that particular day will not count towards the 330-day test. The burden is on the taxpayer to keep a proper calendar of where his or her days were spent. The test is not deemed fulfilled until the 330th day of presence in the foreign country over a 12-month period.

Both tests require the taxpayer to establish residence or presence over the period of a year. A taxpayer might not meet the requirements for the exclusion by the time his or her tax return is due if the taxpayer arrived in the foreign country in the middle of the year. This may preclude a taxpayer from electing to exclude the income on a timely filed return.

Fortunately, the regulations provide for an extended period during which the taxpayer may make the election to exclude foreign earned income. However, the extended period applies only for the purpose of making the election and not for the purpose of filing his return (tax is always due by the original due date, April 15th). Thus, the taxpayer may want to file a return by the due date and then amend to take advantage of the exclusions.

The FEIE is subject to an inflation adjusted limitation. For 2010, the maximum exclusion amount for a full year is $91,500 ($91,400 for 2009). However, the exclusion amount is further limited to a pro rata portion of the annual exclusion based on the days in the year the taxpayer is qualified for the exclusion. The FHE is also subject to a limitation which is determined based on the allowable FEIE for the year.

We can provide you with guidance and consultation to help you unravel the tax complications of working abroad. For questions, please contact Director of International Tax Julia Gowe at (212) 697-6900, JGowe@hrrllp.com or your Holtz Rubenstein Reminick tax adviser.

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