MIRROR, MIRROR, ON THE WALL, WHICH IS MY TAX HOME OF THEM ALL? – FOREIGN STUDENTS FACE DILEMMA IN THE U.S.

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INTRODUCTION

Not all is exciting when a foreign student gets a job offer from a U.S. employer under the Summer Work Travel Program administered by the U.S. Department of State. While the student is busy getting his or her ducks in a row, he or she should not forget about the tax nitty-gritty of arriving and working in the U.S. This article discusses the deductibility of travel expenses incurred by a foreign student who arrives in the U.S. on a J-1 visa under the Summer Work Travel Program.

THE TRI-F(A)CTA FOR THE TRAVEL EXPENSE DEDUCTION

The U.S. Department of State administers the Exchange Visitor Program, which designates sponsors to provide foreign nationals with opportunities to participate in educational and cultural programs in the U.S. and return home to share their experiences. One component of the Exchange Visitor Program is the Summer Work Travel Program (the "Program"), which provides foreign students with the opportunity to work in the U.S. Foreign students must apply for a J-1 visa to enter the U.S. and work under the Program.

Generally, a foreign individual employed and performing personal services within the U.S. is considered to be engaged in a U.S. trade or business and is, therefore, subject to U.S. Federal income tax.[1] A nonresident alien individual who is temporarily present in the U.S. under an F or J visa, and who otherwise is not engaged in a trade or business in the U.S., is nevertheless deemed to be engaged in a trade or business in the U.S. during the tax year.[2] Accordingly, income earned by foreign students while working in the U.S. under the Program is subject to U.S. Federal income tax. However, the U.S. has entered into tax treaties with several countries that offer tax benefits to J-1 visa holders. For example, a student or business apprentice may be exempt from tax on wages received while studying or training up to an annual dollar limit,[3] and a teacher or a research scholar may be exempt from tax on all of their wage income paid by a U.S. educational or research institution for up to two years. These exemptions are subject to

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1 Code §864(b) (an exception applies to the performance of services for a foreign employer for not more than 90 days in the aggregate throughout a taxable year and compensation not exceeding $3,000 in the aggregate); Code §871(b)(1).

2 Treas. Reg. §1.871-9(a).

3 *E.g.*, Article 21(1) of the U.S.-France Income Tax Treaty (exclusion of up to $5,000 of compensation for a foreign student). An exception under domestic law is limited to holders of F, J, and Q visas and is subject to the condition that the student must be paid by a foreign employer (Code §872(b)(3)).

several conditions. Where these exemptions are not available, the Code also offers several deductions that, in turn, reduce the tax liability. Among other deductions, the Code allows a deduction if the expense meets three conditions:

- It is ordinary and necessary and is incurred in carrying on any trade or business.
- It is incurred while away from home.
- It is incurred in the pursuit of a trade or business.[4]

"A taxpayer's 'home' is his or her 'principal place of business or employment.'"

As mentioned above, a foreign student providing personal services in the U.S. usually satisfies the first condition of "carrying on a U.S. trade or business." Travel expenses usually meet the "ordinary and necessary" test.

Recently, in the case of *Richard Liljeberg v. Commr.*,[5] the U.S. Court of Appeals for the District of Columbia Circuit discussed the second and the third conditions of Code §162(a)(2) in the context of three non-U.S. citizens students who visited and worked in the U.S. for few months under the Program.

The students entered the U.S. on J-1 visas. They incurred travel expenses, which included airfare to and from the U.S. to their respective home countries, the cost of the Program, visa costs, and insurance. The students reported their wages on U.S. Federal income tax returns and also deducted the travel expenses on the grounds that they incurred the expenses while they were away from home in the pursuit of a U.S. trade or business.

At a first glance, the word "home" in the phrase "away from home" (under the second condition) may be understood as the employee's place of residence. However, the I.R.S., the Tax Court, and the majority of U.S. circuit courts have adopted the position that a taxpayer's "home" is his or her "principal place of business or employment."[6] The interpretation is based on the premise that an average taxpayer maintains a home close to his place of employment.[7] Thus, taxpayers who incur travel expenses because they maintain their residence at a place other than their principal place of business is ineligible to deduct these expenses.

In *Richard Liljeberg*, the court interpreted the word "home" used in Code §162(a)(2) in the same manner. The issue at the heart of the case was the foreign students' location, for tax purposes, during the Program. If their foreign homes were their tax homes, then the "away from home" requirement would be satisfied and the travel expenses would be deductible. However, if their summer job sites in the U.S. constituted their tax homes, then they were not away from home and could not deduct the expenses. The court held that the students were not "away from home" because they lacked a business reason to maintain a distant, separate residence away from their principal place of employment and so could not claim a personal residence as

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4 Code §162(a)(2).

5 No. 17-1204 (D.C. Cir. Nov. 2, 2018).

6 Revenue Ruling 63-82. However, a few courts have held that "home" means a taxpayer's usual residence. In *Rosenspan v. U.S.*, 438 F.2d 905, 911-12 (2d Cir. 1971), the Second Circuit concluded that "when Congress uses such a non-technical word in a tax statute, presumably it wants administrators and courts to read it in the way that ordinary people would understand."

7 *Bixler v. Commr.*, 5 B.T.A. 1181, 1184 (1927).

a tax home. Further, the students did not have any business connections with their respective home countries (none of them where employed) and, therefore, could not have been away from home. The fact that their J-1 visas required them to keep a foreign residence did not mean their foreign residence qualified as a home for tax purposes, as the immigration law did not specifically require them to keep a second home in their home country.

Further, the court also held that failure to satisfy any one of the three conditions jeopardizes the travel expense deduction under Code §162(a)(2). Thus, even if the students were away from home, the travel expenses would be deductible only if the "in pursuit of business" requirement was met. This requirement is satisfied only when the employer's business forces the taxpayer to travel and to live temporarily at some place other than their usual residence to advance the interests of the employer. The exigencies of the business, rather than the personal conveniences and necessities of the traveler, are the motivating factors.[8]

The court referred to *Flowers*[9] and observed that the third condition requires a direct connection between the expenditure and the carrying on of the taxpayer's or the employer's trade or business. Expenses incurred solely as the result of the taxpayer's desire to maintain a home in one place while working in another are irrelevant to the maintenance of the employer's business. In the case of the foreign students, the court held that the U.S. employers did not require them to move to the U.S.; rather, the students chose to come to the U.S. to participate in the Program. Therefore, the travel expenses flowed from that personal choice rather than the exigencies of the employers. Consequently, the deduction of the travel expenses incurred in connection with the Program was disallowed.

CONCLUSION

It is sad but true that U.S. tax law can turn the thrill of coming to the U.S. into agony when it comes time to file tax returns. Foreign students may not be able to deduct expenses for travelling to the U.S. under the Program; however, not all is lost in the antagonism between foreign students and the I.R.S.

Foreign students may still be able to claim an exemption on their wages, either up to a certain dollar limit or for a specified period under a relevant tax treaty. Thus, although it may seem a dispensable cost, it may be worthwhile for foreign students to engage the services of a tax professional to ensure they do not leave money on the table.

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8 *Commr. v. Flowers*, 326 U.S. 465, 470 (1946).

9 *Id.*