

Online Resource

Federal Taxation Essentials for International Students in the U.S

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Sprintax™

Each year, a large number of international students look to benefit from a widely recognized education in the United States. An Institute of International Education report (2013) disclosed that the number of international students at colleges and universities in the United States increased by 6-7% to a record high of 764,495 in the 2011/12 academic year compared to the year before.

A significant increase is represented by Chinese students where the overall percentage is over 20% higher. The countries with the largest number of international students attending US universities are: China, India, Canada, Japan, and Mexico. A large increase has also been reported in the volume of students from Saudi Arabia.

This growth in the numbers of international students has resulted in a significant positive impact on the United States economy. To date, the financial contribution is more than \$22 billion to the US, according to the US Department of Commerce. More than 30% of the funds received by international students are generally brought by scholarships and grants provided by US Government and Educational institutions under special student programs. Other US income sources are derived from campus employment payments, graduate assistantship and compensation for training.

Employment Opportunities for International Students

For the most part, international students work at the colleges as part time employees. According to the US Citizenship and Immigration Services (USCIS) employment rules, international students on visa (F-1 students) may not work off-campus, but may accept on-campus part-time employment. However, international students may engage in practical training, and earn income through one of the USCIS approved programs discussed below.

There are a few programs available for F-1, J-1, M-1 students and other types of visa holder students which allow them to participate in off-campus employment during or post-study. Off-campus employment must be related to their area of study and must be



authorized prior to starting any work by the official authorized to maintain the Student and Exchange Visitor Information System (SEVIS) and USCIS.

During or post completion of their study, international students may engage in three types of off-campus employment for the rest of their study:

- Curricular Practical Training (CPT)
- Optional Practical Training (OPT)
- Optional Practical Training Extension (OPT) for Science, Technology, Engineering, and Mathematics (STEM) students

In the United States, all employees are required to pay tax. Many international students may not be familiar about paying income tax because such practice is not implemented in their home countries.

Types of Taxes for International Students: Treaties and Taxation

For many international students, the US tax system may seem complex and as a result they are not aware of their filing and taxation obligations. The US tax system involves two main levels of taxation: federal and state. As foreign students under F1, M1, J1 and Q visas are generally considered to be engaged in a trade or business, they are usually liable to pay both federal and state taxes on their US sourced income, which may include wages, tips, scholarship and fellowship grants, dividends, and so on.

In comparison to US residents and citizens, non-resident aliens (including students, trainees, scholars and etc.) are not liable to report and pay tax on their income from outside the US as long as they are considered non-resident aliens. In addition, special rules apply to the taxation of foreign students and scholars which do not apply to other kinds of aliens.

As a part of the federal tax system, US income is in principle subject to FICA (Social Security and Medicare taxes) as well. Non-resident alien students, scholars, professors, teachers, trainees, researchers, physicians and other aliens temporarily present in US on F-1, J-1, M-1, or Q-1/Q-2 visas are exempt from this tax as long as they are treated as non-resident aliens for federal tax purposes and this employment is allowed by USCIS for their visa and program type.

Federal tax filing requirements: Specific taxation rules for students

Residency for tax purpose

Determining your residency status is essential for ensuring your tax liability is accurately assessed and reported. Foreign nationals are subject to one of the three residency status tests for federal tax purposes: Green Card Holders, US Citizenship and residence based on Substantial Presence. Holding a Green card or US citizenship status



means you will be deemed a resident for tax purposes and be subject to the same taxes and tax rates as any other US Citizen. The ‘Substantial Presence Test’ on the other hand calculates the total amount of time you’ve spent in the US over the last three years to determine your status. To pass the Substantial Presence Test, the applicant must have been present for a cumulative total of 183 days over a three-year period. The applicant may include in the count, all of the days they are present in the US in the year of application, 1/3 of the days they were present from the previous year and a 1/6 of the days present in the year prior to this.

Students on both J-1 and F-1 visa are considered “exempt” individuals for the first five years they are physically present in the US which means that they do not need to perform any of the residency tests in this period and are automatically considered ‘non- resident aliens for federal tax purposes’.

Example:

Katarina is citizen of Russia studying in the US full time on an F1 visa. She entered the US on 08-08-2007, exited the US on 05-08-2012 and did not change her visa and immigrant status since then. Her residency status for 2012 is determined as follows:

Katarina is an exempt individual for purposes of the Substantial Presence Test (SPT) for the first five years and so does not count her presence in the US from 2007 – 2011. In 2012, her 6th year of presence, she starts to count days for the purposes of the SPT as follows:

2012: 128 days (by 05-08-2012)
2011: 0 days (exempt individual)
2010: 0 days (exempt individual)

Her total number of days for SPT is 128, so Katarina is still considered nonresident alien in her 6th year of presence.

Tax filing requirement for non-resident aliens

Non-resident aliens file form 1040NR-EZ or 1040-NR “US Non-Resident Alien Income Tax Return” to assess and file federal income and taxes. Most non-resident aliens do not qualify for the standard deduction. If the gross earned income from sources within the US does not exceed the personal exemption allowance of \$3,800.00 in 2012 or \$3,900.00 in 2013, a federal income tax return is not due. The filing threshold equals one personal exemption and is adjusted annually for inflation.

It is important to note that each individual state has its own tax system and tax regulations imposing different residency and filing requirements under which foreign students may have to file state tax return though no federal return is due.



Scholarship income treatment

Scholarships and Fellowship Grants are taxable income when paid to non-resident aliens. IRS Notice 87-31 exempts scholarships and fellowships from tax in the US when paid to US citizens and residents, yet the US scholarship and fellowship grants paid directly to a foreign student are generally taxable and subject to reporting.

The general rule is that you cannot deduct personal or living expenses, unless specifically allowed by the code. In addition, non-resident aliens are generally restricted from the standard deduction, as it applies solely to residents. However the option to claim itemized deduction still stands. For instance, students may claim all state and local taxes withheld through payroll or paid directly to the state tax authorities during the fiscal year as deduction on their federal tax return. Contributions made to qualified charities are also deductible. Some ordinary and necessary job related, income producing or conserving expenses are also deductible to the extent that they exceed the 2 percent of adjusted gross income floor. These include, but are not limited to, union dues, job search expenses, tax return preparation fees and unreimbursed employee business expenses.

Some so-called "above the line" deductions (deductions subtracted from the gross income before the adjusted gross income is calculated for tax purposes) could bring substantial benefit to those who are recipients of a scholarship or fellowship grant. Under Internal Revenue Code Section 117, foreign students are eligible for a direct write-off of that part of the grant that was used to cover qualified educational expenses. The deduction applies to all non-resident aliens who are candidates for a degree or at least half-time students. The qualified educational expenses include all out-of-pocket expenses paid for tuition, academic fees, books, supplies and equipment required by a college or university.

International students may also avail of a tax treaty which will allow them to exempt fully or partially their US sourced income from federal and/or state tax. The US tax treaty network covers more than 65 countries and almost all treaties have specific provisions that apply to students, trainees and apprentices. Attention should be paid as certain states do not always follow the federal treaties.

Ways to Pay Tax: Machines, Software or Websites?

In the event that the taxpayer has underpaid their federal income tax, they can pay their outstanding tax amount to the IRS by:

- Debit or credit card
- Electronic funds transfer
- Check or money order

For cases where the taxpayer is not in position to transfer the full amount of federal income tax payment to the IRS, taxpayers may participate in an IRS program



and pay their taxes over an extended period of time through applying for an Installment Agreement. The participants in the Installment Agreement program can choose their monthly payment amount and pay their tax over 24 month period. However, the IRS does impose an additional fee for the organization of this agreement.

Commercial Services: Sprintax and Benefits

Nina Olson, National Taxpayer Advocate, summarizes the conclusion of the National Taxpayer Advocate states as follows: “The existing tax code makes compliance difficult, requiring taxpayers to devote excessive time to preparing and filing their returns, and leaving many unaware how their taxes are computed and even what rate of tax they pay” Moreover, the taxation and filing rules significantly differs between US residents and non-resident aliens. As a result many international students and non-resident aliens face serious difficulties in determining their filing and taxation obligations. They have the choice to visit the IRS website to gather information on their individual tax obligations. Because the non-resident tax forms are not provided in electronic submission format, most online (e-file) tax return providers do not support the required non-resident forms 1040NR and 1040NR-EZ.

Software solutions like Sprintax.com™ do, and have been specifically designed to serve international students. Sprintax.com™ makes tax preparation quick and easy and provides full 24/7 customer help through a live chat system and toll-free number for students to call if they have questions. Sprintax.com™ is web-based, so international students can log in from anywhere. Students complete the simple step-by-step questionnaire and Sprintax.com™ populates the tax return forms. The student receives the completed tax return by email and simply has to check, print, sign and post directly to the IRS.

Sprintax.com™ provides non-resident tax form preparation service by presenting individuals with a comprehensive questionnaire which will determine their residency status. The software analyzes personal, income and tax information and produces non-resident tax forms as 1040NR, 1040NR-EZ, 8843 form, W-7 ITIN application where applicable. Through user-friendly, step-by-step application, the software collects data that serve to consider the allowed expenses, tax treaty benefits, deductions and exemptions in each individual case helping the user to prepare a compliant tax return and reduce income tax liability as much as is legally possible. Sprintax website: <https://www.sprintax.com/>

Conclusion

International students and non-residents face tax payment and filing obligations on most of their income. Typically, they need to submit annual tax return on forms 1040NR and 1040NR-EZ. They may need to consider many personal details: program and visa related factors as well as a considerable number of income types and taxes with the relevant federal and state tax authorities. Many foreign students may still feel uncertain

about their tax position and may seek advice from a tax professional or avail of an online tax preparation software provider to do the job on their behalf.

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