DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

March 6, 2000

Number: **200017043**
Release Date: 4/28/2000
CC:INTL:BR1
WTA-N-103730-99
UILC: 9114.03-22

INTERNAL REVENUE SERVICE NATIONAL OFFICE TECHNICAL ASSISTANCE

MEMORANDUM FOR DAVID C. LUMBRERAS
AIR TRANSPORT INDUSTRY SPECIALIST
4300 MSRO

FROM: M. GRACE FLEEMAN
Assistant to the Branch Chief
CC:INTL:Br1

SUBJECT: Treatment of FICA under the U.S.-Japan income tax treaty

This Technical Assistance responds to your memorandum dated February 11, 1999. Technical Assistance does not relate to a specific case and is not binding on Examination or Appeals. This document is not to be used or cited as precedent.

ISSUES:

Issue 1:

Does the employee portion of the FICA tax that is imposed under section 3101 of the Internal Revenue Code of 1986, as amended (the "Code"), constitute a covered tax under Article 1, paragraph (1) (a) of the U.S.-Japan income tax convention (the "Treaty") [1] ?

Issue 2:

If the employee portion of the FICA tax is a covered tax, will application of the Treaty reduce the FICA tax liability of a flight attendant who is a resident of Japan, employed on a U.S. aircraft as part of the regular compliment of the aircraft, and whose contract of employment was entered into in the United States?

---

[1] Convention Between the United States of America and Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion With Respect to Taxes on Income, March 8, 1971 (1972), 23 U.S.T. 967, 1973-1 C.B. 630.

Issue 3:

Does the employer portion of the FICA tax that is imposed under section 3111 of the Code constitute a covered tax under Article 1, paragraph (1)(a) of the Treaty?

CONCLUSIONS:

Issue 1:

Because the employee portion of the FICA tax is a Federal income tax and there is no evidence that it was intended to be excluded from coverage by the Treaty, we believe the better view is that is should be treated as a covered tax.

Issue 2:

Although the employee portion of the FICA tax is a covered tax, application of the Treaty will not reduce the FICA tax liability of a flight attendant who is a resident of Japan, employed on a U.S. aircraft as part of the regular compliment of the aircraft, and whose contract of employment was entered into in the United States.

Issue 3:

The employer portion of the FICA tax is an excise tax and, as such, it does not constitute a covered tax under Article 1, paragraph (1)(a) of the Treaty.

FACTS:

You have requested assistance in interpreting the impact of the Treaty on the FICA tax liability of both the employee and the employer in the following scenario.

> In order to provide better service to non-English speaking passengers traveling on international routes, U.S. air carriers are employing some flight attendants who speak foreign languages. The U.S. air carriers require such flight attendants to generally be "based in" a foreign country on an international route.[2] For example, Japanese speaking flight attendants are based in Japan to provide better service to Japanese speaking passengers.

---

[2] The airline industry uses the term "domiciled" to describe a flight attendant that is assigned to work out of a particular city. The term "domicile" can have specific meanings under the Code and the regulations thereunder, as well as under foreign law, and these meanings can vary from the industry usage. This memorandum uses the concept of "based in" a particular city or country rather than the term "domiciled" to avoid confusion.

These flight attendants are residents of Japan for purposes of Japanese tax and are employed as a part of the regular complement of the crew of an American aircraft operated by a U.S. air carrier on flights between the United States and Japan. The flight attendants entered into their contracts of employment in the United States.

LAW AND ANALYSIS:

The Code

The social security or FICA tax is imposed under the Federal Insurance Contributions Act, which is contained in Chapter 21 (sections 3101 et seq.) of the Code. The employee portion of the tax is imposed under section 3101, and the employer portion is imposed under section 3111.

Section 3101(a) and (b) imposes on the income of all individuals additional taxes equal to specified percentages of the "wages" (as defined in section 3121(a)) they receive with respect to "employment" (as defined in section 3121(b)). Section 3102 requires the individuals' employers to collect the taxes imposed by section 3101 by deducting the amount of such taxes from the wages as and when paid. Section 3111(a) and (b) imposes matching excise taxes on the employers.

The term "wages" is generally defined in section 3121(a) as all remuneration paid to an employee with respect to his employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash. There are several enumerated exceptions (not applicable here) and, in the case of the taxes imposed by sections 3101(a) and 3111(a), an annual earnings ceiling above which the tax is not imposed.

The term "employment" is defined in section 3121(b) to include, in pertinent part, any service performed by an employee for a person employing him, irrespective of the citizenship or residence of either, if such service is performed either (1) within the United States, or (2) on or in connection with an American aircraft if either (a) the contract of service was entered into in the United States, or (b) during the performance of which and while the employee is employed on the aircraft it touches at a port in the United States, if the employee is also employed on and in connection with such aircraft when it is outside the United States. Section 3121(f) provides that an American aircraft is an aircraft registered under the laws of the United States.

The Treaty

Article 1 (Taxes Covered), paragraph (1)(a) of the Treaty provides that "[t]he taxes which are the subject of this convention are: (a) In the case of the United States,

the Federal income taxes imposed by the Internal Revenue Code, hereinafter referred to as 'United States tax'..."

Article 2 (General Definitions), paragraph (2) of the Treaty provides that any term used in the Treaty and not otherwise defined shall, unless the context otherwise requires, have the meaning which it has under the laws of that Contracting State relating to the taxes which are the subject of the convention.

Under paragraph (1) of Article 3 (Resident) of the Treaty, a "resident of Japan" includes an individual who is resident in Japan for purposes of Japanese tax. We assume the flight attendants in this case who are based in Japan are residents of Japan for purposes of the Treaty.[3]

Paragraph (1) of Article 4 (Scope) of the Treaty provides the following general rule:

> A resident of a Contracting State may be taxed by the other Contracting State on any income from sources within that other Contracting State and only on such income, subject to any limitations set forth in this Convention. For this purpose, the rules set forth in Article 6 shall be applied to determine the source of income.

Paragraph (6) of Article 6 (Source of Income) of the Treaty provides in relevant part that "[i]ncome from labor or personal services performed aboard ships or aircraft operated by a resident of a Contracting State in international traffic shall be treated as income from sources within that Contracting State, if rendered by a member of the regular complement of the ship or aircraft."

Paragraph (1) of Article 18 (Dependent Personal Services) of the Treaty provides in relevant part that, subject to an exception not applicable here, wages, salaries, and similar remuneration derived by an individual who is a resident of a Contracting State from labor or personal services performed as an employee may be taxed by the other Contracting State to the extent the remuneration is derived from sources within the other Contracting State.

Issue 1:

As stated above, Article 1 (Taxes Covered), paragraph (1)(a) of the Treaty provides that "[t]he taxes which are the subject of this convention are: (a) In the case of the United States, the Federal income taxes imposed by the Internal Revenue Code, hereinafter referred to as 'United States tax.'" The Treaty is silent on the issue of

---

[3] We assume the flight attendants are not also residents of the United States within the meaning of paragraph (2) of Article 3.

whether FICA is a covered tax, and the Treasury Department's Technical Explanation of the Treaty ("Technical Explanation") is also silent. In other, more recent U.S. income tax treaties, where FICA was not intended to be a covered tax, this has been explicitly stated either in the treaty itself [4] or in the technical explanation.[5] It appears the drafters of such treaties believed the employee portion of the FICA tax would be a covered tax unless specifically excluded. We have found no evidence that the parties to the Treaty intended to exclude social security taxes from coverage by the Treaty.

Under Article 2, paragraph 2, if a term is not defined in the Treaty, we must look to U.S. law for the meaning of terms relating to taxes imposed by the United States. The Code in several places refers to the employee portion of the FICA tax as an income tax.[6] The United States Supreme Court also referred to the employee portion of the FICA tax as an income tax on employees when it upheld the constitutionality of FICA in 1937.[7] Thus, the employee portion of the FICA tax is considered an income tax under both the Code and domestic case law.

Accordingly, although the employee portion of the FICA tax is not specifically identified in the Treaty as a covered tax, we believe the better view is that the employee portion of the FICA tax that is imposed under section 3101, is a covered tax under Article 1, paragraph (1) (a) of the Treaty.

Issue 2:

The United States and Japan have not entered into a Social Security totalization agreement. Therefore, the only bilateral agreement that could potentially reduce the FICA tax liability of an individual flight attendant based in Japan would be the Treaty.

---

[4] See, for example, the treaties currently in force with Austria, France, Germany, Ireland, and the Netherlands.

[5] See, for example, the treaties currently in force with Australia, Italy, and the Philippines.

[6] Section 3101, which imposes the FICA tax on employees, provides that the tax "is hereby imposed on the *income* of every individual...equal to the following percentages of the wages... received by him with respect to employment" (emphasis added). Similarly, section 275(a)(1) disallows a deduction for federal income tax purposes for "federal income taxes, including...the tax imposed by section 3101."

[7] *Helvering v. Davis*, 301 U.S. 619, 635 (1937).

Article 6 (Source of Income), paragraph (6) and Article 4 (Scope), paragraph (1) of the Treaty together provide that, subject to any limitations elsewhere in the Treaty, residents of Japan who are members of the regular complement of an aircraft operated by a U.S. resident in international traffic may be taxed by the United States on all of the income they derive from services performed aboard the aircraft. Because 100 percent of the remuneration for services performed aboard the aircraft in this case will be treated as derived from sources within the United States, paragraph (1) of Article 18 (Dependent Personal Services) allows the United States the right to impose a covered tax, including FICA, on 100 percent of the remuneration paid by the U.S. air carrier to the flight attendants for such services. The Treaty provides no specific exemption from or reduction in the rate of the FICA tax.

As stated above, the employee portion of the FICA tax is imposed by section 3101(a) and (b) on the income of all individuals in an amount equal to specified percentages of the "wages" (as defined in section 3121(a)) they receive with respect to "employment" (as defined in section 3121(b)).

The term "employment" is defined in section 3121(b) to include, in pertinent part, any service performed by an employee for a person employing him, irrespective of the citizenship or residence of either, if such service is performed on or in connection with an American aircraft if the contract of service was entered into in the United States. Under the facts outlined above, the flight attendants are employed on an American aircraft and their contracts for employment were entered into in the United States. Therefore, 100 percent of the remuneration paid to the employees for services performed on the American aircraft (other than any amounts above the applicable annual earnings ceiling) is treated as wages from employment and is subject to FICA under section 3101 and section 3111.

Because the Treaty provides for no specific exemption from or reduction in the rate of the FICA tax and because the entire amount of "wages" received by the flight attendants under the facts provided will be taxable by the United States under the Treaty and subject to FICA under section 3101 of the Code, application of the Treaty would not reduce the amount of the flight attendant's FICA tax liability.

Issue 3:

As stated above, Article 1, paragraph (1)(a) of the Treaty provides that "[t]he taxes which are the subject of this convention are: (a) In the case of the United States, the Federal income taxes imposed by the Internal Revenue Code, hereinafter referred to as 'United States tax'..." The employer portion of the FICA tax is not an

income tax but an excise tax,[8] which is measured not by the employer's own income but by the income of the employees. Therefore, it is clearly not covered by the Treaty. Because the Treaty does not apply to the U.S. air carrier's liability for the employer portion of the FICA tax, the normal Code rules apply.

If you have any further questions, please call (202) 622-3880.

M. GRACE FLEEMAN
Assistant to the Branch Chief
Branch 1
Office of the Associate Chief Counsel
(International)

[8] Section 3111(a) ("there is hereby imposed on every employer an *excise* tax") (emphasis added). See also, *Stewart Machine Co. v. Davis*, 301 U.S. 548 (1937), at 578-583.