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

OFFICE OF CHIEF COUNSEL

2/27/2004

Number: **INFO 2004-0080**
Release Date: 6/30/2004
CONEX-104346-04/CC:INTL:B01
Index: 9999.00-00

[redacted]

Dear [redacted]:

This letter is in response to your request for income tax information concerning non-U.S. military members and their spouses who reside in the United States under a North Atlantic Treaty Organization (NATO) visa. You asked for information about the appropriate tax return filing status, inclusion of amounts in gross income, and the availability of certain tax credits when a non-U.S. military member's income is exempt from U.S. taxation under Article X(1) of the Agreement Between the Parties to the North Atlantic Treaty Regarding the Status of their Forces ("NATO SOFA" or "SOFA").

Q.1(a). Can a NATO dependent spouse use the filing status of "single"?

The marital status of every individual required to file a federal income tax return is determined by the individual's status on the last day of his or her tax year, which is December 31 for most taxpayers. § 7703(a)(1) of the Internal Revenue Code (the Code). Thus, a taxpayer who is married and lives with his or her spouse on the last day of the tax year is considered married for tax purposes. The tax return filing options available to a taxpayer who is married are "married filing a joint return" or "married filing a separate return." Because no provision of the NATO SOFA changes this filing status requirement, a NATO dependent spouse can not elect to file as a single taxpayer.

Q.1(b). If a non-U.S. military member present in the U.S. and his or her NATO dependent spouse file a joint return, (i) must the non-U.S. military member's NATO SOFA income be included in the joint return; and (ii) is the non-U.S. military member considered a resident alien?

If a non-U.S. military member residing in the U.S. and his or her NATO dependent spouse elect to file a joint return, the member's NATO salary would remain exempt from tax and would not be reported on their joint return. Further, if they file a joint return, the non-U.S. military member is considered a resident alien.

A non-U.S. citizen is a resident alien if he or she meets the substantial presence test described in § 7701(b)(3) of the Code. The first paragraph of Article X(1) of the NATO SOFA makes clear that the period in which a non-U.S. member is in the U.S. solely for purposes of performing his or her official duties is not taken into account in determining whether he or she satisfies the substantial presence test.1 (*See* § 894(a)(1) of the Code, which provides that the provisions of the Code shall be applied to any taxpayer with due regard to any treaty obligation of the United States which applies to such taxpayer.) Only those days in which the non-U.S. military member is in the U.S. for reasons other than the performance of his or her official duties would be considered for purposes of the substantial presence test.

Even if a non-U.S. military member does not meet the substantial presence test, the member may file a joint return if the member's NATO dependent spouse is a resident alien. Article X(1) of the SOFA does not address the residence or domicile of the member's dependents. A NATO dependent spouse will therefore be a resident alien under the substantial presence test if the spouse is in the United States for a sufficient number of days. Although days of presence as a member of the immediate family of a full-time employee of an international organization are excluded for purposes of the substantial presence test, NATO is not an international organization for this purpose. §§ 7701(b)(3)(D)(i), (5)(A)(i), and (5)(B)(ii)-(iii) of the Code. *See also* Treas. Reg. § 301.7701(b)-3(b)(2)(ii) (defining "international organization" as "any public international organization that has been designated by the President by Executive Order as being entitled to enjoy the privileges, exemptions, and immunities provided for in the International Organizations Act (22 U.S.C. § 288)").

If the NATO dependent spouse is a resident alien because he or she is in the United States for a sufficient number of days, the spouse must file a Form 1040 as a resident alien (unless, as discussed in Q.6 below, he or she claims benefits as a resident of another country under an income tax treaty with the United States). The correct filing status would be "married filing separately" rather than "single" unless the spouses elect to file a joint return under § 6013(g) of the Code.

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1 The first paragraph of Article X(1) of the NATO SOFA provides that "[w]here the legal incidence of any form of taxation in the receiving State [here the United States] depends upon residence or domicile, periods during which a member of a force or civilian component is in the territory of that State by reason *solely* of his being a member of such force or civilian component shall not be considered as periods of residence therein, or as creating a change of residence or domicile, for the purposes of such taxation" *(emphasis added)*.

If the NATO dependent spouse is a resident alien by virtue of the substantial presence test, the NATO dependent spouse and the non-U.S. military member may elect to file a joint return even if the member does not meet the substantial presence test. § 6013(g) of the Code. If they make this election, then the non-U.S. military member is treated as a resident of the United States for purposes of chapter 1 of the Code for all of such tax year. § 6013(g)(1)(A) of the Code. Even if the non-U.S. military member is treated as a resident of the United States by reason of an election under § 6013(g) of the Code, the member's NATO salary would remain exempt from tax under Article X(1) of the SOFA, which provides that "[m]embers of a force or civilian component shall be exempt from taxation in the receiving State on the salary and emoluments paid to them as such members by the sending State or on any tangible movable property the presence of which in the receiving State is due solely to their temporary presence there."

Q.1(c). Can a NATO dependent spouse use the "head of household" filing status?

The head of household filing status is available only to an individual who is not married as of the end of the tax year and who maintains as his or her home a household that constitutes for more than one-half of such tax year the principal place of abode of an unmarried child as a member of that household. § 2(b) of the Code. Because a NATO dependent spouse is not considered unmarried at the close of the taxable year, he or she can not file as a head of household.

Q.1(d). Can a "resident" NATO dependent spouse use the "married filing separately" filing status?

A taxpayer who is married at the end of the taxable year can elect to file a separate income tax return using the married filing separately status.

Q.2. Can a NATO dependent spouse claim his or her children as dependents for exemption purposes?

Generally, an individual may claim another as a dependent on his or her federal income tax return if he or she satisfies five tests. These tests are: (1) the member of household or relationship test, (2) the joint return test, (3) the citizen or resident test, (4) the income test, and (5) the support test.

If the dependent is a child of the NATO dependent spouse, the member of household or relationship test would be met for that child. Further, to be claimed as a dependent by the NATO dependent spouse, the child must not have filed a joint return and must be a U.S. citizen or resident, or a resident of Canada or Mexico, for some part of the NATO dependent spouse's tax year. The NATO dependent spouse meets the income

test for any child who is under 19, or under 24 and a full-time student. Finally, without a multiple support agreement or a child of divorced or separated parents, the NATO dependent spouse must provide more than half of a child's total support during the calendar year to meet the support test. To figure whether a person has provided more than half of a child's total support, the person must compare the amount he or she contributed to the child's support with the entire amount of support that child received from all sources, including support the child provided from his or her own funds. Although the salary earned by the non-U.S. military member is exempt from tax, that amount is considered in the support test of a child if it is used to support the child. Consequently, if a NATO dependent spouse files a married filing separately return, he or she would most likely not meet the support test for a child if the NATO dependent spouse's income is significantly less than the income of the non-U.S. military member. Conversely, if they file a joint return, the spouses would likely meet the support test for their child.

A taxpayer must list the social security number (SSN) of any person for whom he or she claims a dependency exemption. If the dependent is a resident or nonresident alien who does not have and is not eligible to get an SSN, the dependent must apply for an individual taxpayer identification number (ITIN).

Q.3. Can a NATO dependent spouse claim the non-U.S. military member as a dependent for exemption purposes?

A spouse is never a dependent for federal income tax purposes.

Q.4. Is a NATO dependent spouse eligible for the earned income tax credit?

To claim the earned income credit (EIC), a taxpayer must meet several eligibility requirements identified in § 32(c)(1) of the Code. An individual who is a nonresident alien for any portion of the tax year is not eligible to claim the EIC unless he or she is married and makes a joint return election under § 6013(g) or (h) of the Code. § 32(c)(1)(E) of the Code.

The Code allows an EIC to an eligible individual only if he or she includes on the tax return the individual's (and spouse's, if filing a joint return) taxpayer identification number (TIN). § 32(c)(1)(F) of the Code. Solely for purposes of the EIC, a TIN is, with certain exceptions not pertinent here, an SSN issued to the individual by the Social Security Administration (SSA). § 32(m) of the Code.

In the case of a married individual, the EIC is available only if the individual and spouse file a joint return. § 32(d) of the Code. Thus, a NATO dependent spouse can claim the EIC only if he or she files a joint return on Form 1040, 1040A, or 1040EZ with the non-U.S. military member, and they both have SSNs. The Social Security Administration is

authorized to issue SSNs to aliens in certain situations. § 205(c)(2)(B) of the Social Security Act (42 U.S.C. § 405(c)(2)(B)). As we understand this provision, the NATO dependent spouse would be entitled to an SSN because he or she is entitled to work in the United States. You are correct that the non-U.S. military member is entitled to receive a "not valid for employment" SSN, but some choose not to do so. The "not valid for employment" SSN issued to these individuals is a valid SSN for purposes of the EIC. To claim the EIC, the non-U.S. military member must apply for and receive an SSN before filing the joint return.

A taxpayer with a qualifying child can claim the EIC. A taxpayer without a qualifying child can also claim the EIC. If a taxpayer has a qualifying child, that taxpayer cannot claim the credit for taxpayers without a qualifying child. A "qualifying child" is one who meets relationship, age, and residency requirements. § 32(c)(3) of the Code. The taxpayer's own child meets the relationship requirement. A child meets the age requirement if he or she is under 19, or under 24 and a full-time student, or any age if permanently and totally disabled. The child meets the residency requirement if he or she has the same residence as the taxpayer in the United States for more than half of the tax year. The child is treated as having the same residence as the taxpayer during periods of temporary absences, such as for education.

Generally, the taxpayer's own school-age child who lives with the taxpayer in the United States for more than half of the taxable year is the taxpayer's qualifying child, even if the child is away at school during part of the U. S. residency.

A taxpayer claiming the EIC with a qualifying child must identify the child on the tax return by name, age, and TIN. § 32(c)(3)(D) of the Code. Schedule EIC is used for this purpose.

The child's TIN, like that of the taxpayer, must be an SSN, not a Foreign Identification Number (FIN). As we understand the SSA's implementation of § 205(c)(2)(B) of the Social Security Act, until 1996, when the IRS began issuing ITINs to aliens unable to receive SSNs, the SSA issued SSNs to aliens who needed an SSN for federal tax purposes. Until 2003, the SSA issued SSNs to aliens living in a state that required an SSN to apply for a driver's license or to register a vehicle. In the past, the SSA also issued SSNs to children who needed an SSN for school. As you pointed out, some older children who are permitted to work are entitled to an SSN.

As a result, a taxpayer may have a qualifying child who has an SSN and one who does not. In this case, the taxpayer can claim the EIC only for the child with an SSN. If the taxpayer has one or more qualifying children, but none of the children has an SSN, the taxpayer cannot claim the EIC.

In addition to the eligibility requirements for the taxpayer and the three requirements for the qualifying child, the statute includes certain income requirements. The taxpayer must have earned income. Earned income for an employee is wages, salaries, tips, and other employee compensation that he or she includes in gross income for the taxable year. § 32(c)(2) of the Code. The NATO dependent spouse's wages (the amount in box 1 of Form W-2) are earned income, but the non-U.S. military member's salary is not. (This is a change in the law effective in tax year 2002.)

The taxpayer's earned income and adjusted gross income (AGI) cannot exceed certain amounts. For tax year 2003, the credit phases out completely when the taxpayer's earned income (or AGI, if higher) reaches $34,692, in the case of a joint return and two qualifying children. The limits are lower for other filing statuses and for taxpayers with fewer than two qualifying children.

The statute also limits the amount of investment income the taxpayer can receive. For tax year 2003, the investment income cannot exceed $2,600. For this purpose, investment income generally includes taxable and tax-exempt interest, dividends, capital gain net income, certain rent and royalty net income, and passive activity net income.

Q.5. Is a NATO dependent spouse entitled to the additional child tax credit for his or her children?

Under certain circumstances, a taxpayer may claim a non-refundable child tax credit to reduce the taxpayer's tax liability. § 24(a) of the Code. For a taxpayer to claim the child tax credit for his or her child, the child must be under age 17 at the end of the tax year, a resident or citizen of the U. S., and claimed as a dependent on the taxpayer's return for the tax year. For tax year 2003, a taxpayer may reduce his or her tax liability by $1,000 for each qualifying child. The $1,000 credit is reduced, however, if the taxpayer reported AGI of $110,000 or more on a jointly filed return or $55,000 or more on a married filing separately return.

A refundable additional child tax credit may be available to a taxpayer who is entitled to take the child tax credit for a child but does not get the full benefit of the credit because the taxpayer's tax liability, before taking the credit into account, is less than the credit. A refundable credit allows a taxpayer to receive a refund even if the taxpayer has no tax liability for the year. A NATO dependent spouse would be entitled to the additional child tax credit only if his or her child is under age 17 at the end of the tax year, a resident or citizen of the United States, and claimed as a dependent on the taxpayer's return for the tax year. If available, the amount of the additional child tax credit would be affected by a number of factors including the amount of qualifying children, the earned income of the taxpayer, the social security taxes paid by the taxpayer, and whether the taxpayer reported an earned income credit.

Q.6. What impact does a tax treaty have on filing options for such personnel?

Treasury Regulations provide special rules for dual resident taxpayers, *i.e.*, alien individuals who are both residents of the United States pursuant to the internal laws of the United States and residents of a treaty country pursuant to the treaty partner's internal laws. § 301.7701(b)-7(a). If an individual is a resident of a foreign country for treaty purposes, and claims a treaty benefit (as a nonresident alien of the United States) to reduce his or her U.S. income tax liability for any income covered by a tax treaty during a tax year when he or she was a dual resident taxpayer, then the law treats that individual as a nonresident alien for purposes of computing the tax liability for the portion of the taxable year he or she was a dual resident taxpayer. Treas. Reg. § 301.7701(b)-7(a)(1).

If a NATO dependent spouse is a resident of a country with which the United States has an income tax treaty in force, the NATO dependent spouse may be able to avoid classification as a resident alien by claiming benefits under the treaty as a resident of the other country. In this case, the NATO dependent spouse would have to file a Form 1040NR rather than a Form 1040. However, classification as a nonresident alien would make the spouse ineligible for the EIC. *See* § 32(c)(1)(E) of the Code (a nonresident alien is not an "eligible individual" unless he or she is treated as a resident of the United States by reason of an election under § 6013(g) or (h)).

Q.7. What substantiation is required when claiming an exemption from tax pursuant to a treaty for income below a certain level?

A taxpayer who takes the position that a treaty of the United States overrules (or otherwise modifies) an internal revenue law of the United States must disclose that position on Form 8833 (Treaty-Based Return Position Disclosure Under Section 6114 or 7701(b)). § 6114(a) of the Code.

Treasury Regulations waive the reporting requirements in a number of situations, including, *inter alia*, the taxation of income derived from dependent personal services. Treas. Reg. § 301.6114-1(c)(1)(iii). Reporting also is waived for an individual if otherwise reportable payments or income items received by the individual during the course of the taxable year do not exceed $10,000 in total. Treas. Reg. § 301.6114-1(c)(2).

Thus, no substantiation is required with respect to remuneration for personal services performed for an employer or in cases where the $10,000 de minimis rule is satisfied. If the individual must provide documentation, he or she should use Form 8833.

Q.8. Must the NATO dependent spouse obtain a certificate of compliance?

Subject to exceptions prescribed by Treasury Regulations, no alien may depart from the United States unless he or she first obtains a certificate indicating that he or she has complied with all the obligations imposed by the income tax laws. § 6851(d) of the Code. The law provides no exception for a NATO dependent spouse.

I hope this information is helpful. We consolidated information from several offices for this response. Please call the primary contact person, [redacted], Identification Number [redacted], at [redacted], if you have any further questions.

Sincerely,

Robert A. Berkovsky
Branch Chief,
Office of Associate Chief Counsel
(Income Tax & Accounting)