*Example 1.* B, a citizen and resident of foreign country F, was engaged in a United States business during 1982 and filed a return on a fiscal year basis. B's fiscal year runs from October 1 to September 30. B comes to the United States on March 8, 1985 and remains in the United States until October 10, 1985, when he returns to country F. B maintains a closer connection to and his tax home in Country F for the remainder of calendar year 1985. B, who is not a United States resident at any time in 1986, is a United States resident for the period that begins on March 8, 1985, and ends on October 10, 1985. B has adopted a fiscal year taxable year for purposes of computing his United States income tax liability. For his fiscal year that ends on September 30, 1985, B will be taxed as a United States resident for the period that begins on March 8, 1985 and ends on September 30, 1985. For his fiscal year that ends on September 30, 1986, B will only be taxed as a United States resident for the period that begins on October 1, 1985 and ends on October 10, 1985.

*Example 2.* The facts are the same as in *Example 1,* except that B's 1982 business was a country F business established on a fiscal year basis and at no time prior to 1985 was B subject to United States income tax. B may adopt a calendar year as his taxable year for United States income tax purposes without requesting a change of accounting period. B continues to use a fiscal year as his taxable year. For his fiscal year that ends on September 30, 1985, B will be taxed as a United States resident for the period that begins on March 8, 1985 and ends September 30, 1985. For his fiscal year that ends on September 30, 1986, B will be taxed as a United States resident for the period that begins on October 1, 1985 and ends on October 10, 1985.

*Example 3.* The facts are the same as in *Example 1,* except that B's 1982 business was a country F business established on a fiscal year basis and at no time prior to 1985 was B subject to United States income tax. B may adopt a calendar year as his taxable year for United States income tax purposes without requesting a change of accounting period. B adopts a calendar year as his taxable year for 1985. For his calendar year taxable year ending on December 31, 1985, B will be taxed as a United States resident for the period that begins on March 8, 1985, and ends on October 10, 1985.

[T.D. 8411, 57 FR 15250, Apr. 27, 1992; 57 FR 28612, June 26, 1992, as amended by T.D. 8996, 67 FR 35012, May 17, 2002]

### § 301.7701(b)–7 Coordination with income tax treaties.

(a) *Consistency requirement*—(1) *Application.* The application of this section shall be limited to an alien individual who is a dual resident taxpayer pursuant to a provision of a treaty that provides for resolution of conflicting claims of residence by the United States and its treaty partner. A ''dual resident taxpayer'' is an individual who is considered a resident of the United States pursuant to the internal laws of the United States and also a resident of a treaty country pursuant to the treaty partner's internal laws. If the alien individual determines that he or she is a resident of the foreign country for treaty purposes, and the alien individual claims a treaty benefit (as a nonresident of the United States) so as to reduce the individual's United States income tax liability with respect to any item of income covered by an applicable tax convention during a taxable year in which the individual was considered a dual resident taxpayer, then that individual shall be treated as a nonresident alien of the United States for purposes of computing that individual's United States income tax liability under the provisions of the Internal Revenue Code and the regulations thereunder (including the withholding provisions of section 1441 and the regulations under that section in cases in which the dual resident taxpayer is the recipient of income subject to withholding) with respect to that portion of the taxable year the individual was considered a dual resident taxpayer.

(2) *Computation of tax liability.* If an alien individual is a dual resident taxpayer, then the rules on residency provided in the convention shall apply for purposes of determining the individual's residence for all purposes of that treaty.

(3) *Other Code purposes.* Generally, for purposes of the Internal Revenue Code other than the computation of the individual's United States income tax liability, the individual shall be treated as a United States resident. Therefore, for example, the individual shall be treated as a United States resident for purposes of determining whether a foreign corporation is a controlled foreign corporation under section 957 or whether a foreign corporation is a foreign personal holding company under section 552. In addition, the application of paragraph (a)(2) of this section does not

affect the determination of the individual's residency time periods under § 301.7701(b)–4.

(4) *Special rules for S corporations.* [Reserved]

(b) *Filing requirements.* An alien individual described in paragraph (a) of this section who determines his or her U.S. tax liability as if he or she were a nonresident alien shall make a return on Form 1040NR on or before the date prescribed by law (including extensions) for making an income tax return as a nonresident. The individual shall prepare a return and compute his or her tax liability as a nonresident alien. The individual shall attach a statement (in the form required in paragraph (c) of this section) to the Form 1040NR. The Form 1040NR and the attached statement, shall be filed with the Internal Revenue Service Center, Philadelphia, PA 19255. The filing of a Form 1040NR by an individual described in paragraph (a) of this section may affect the determination by the Immigration and Naturalization Service as to whether the individual qualifies to maintain a residency permit.

(c) *Contents of statement*—(1) *In general*—(i) *Returns due after December 15, 1997.* The statement filed by an individual described in paragraph (a)(1) of this section, for a return relating to a taxable year for which the due date (without extensions) is after December 15, 1997, must be in the form of a fully completed Form 8833 (Treaty-Based Return Position Disclosure Under Section 6114 or 7701(b)) or appropriate successor form. See section 6114 and § 301.6114–1 for rules relating to other treaty-based return positions taken by the same taxpayer.

(ii) *Earlier returns.* For returns relating to taxable years for which the due date for filing returns (without extensions) is on or before December 15, 1997, the statement filed by the individual described in paragraph (a)(1) of this section must contain the information in accordance with paragraph (c)(1) of this section in effect prior to December 15, 1997 (see § 301.7701(b)–7(c)(1) as contained in 26 CFR part 301, revised April 1, 1997).

(2) *Controlled foreign corporation shareholders.* If the taxpayer who claims a treaty benefit as a nonresident of the United States is a United States shareholder in a controlled foreign corporation (CFC), as defined in section 957 or section 953(c), and there are no other United States shareholders in that CFC, then for purposes of paragraph (c)(1) of this section, the approximate amount of subpart F income (as defined in section 952) that would have been included in the taxpayer's income may be determined based on the audited foreign financial statements of the CFC.

(3) *S corporation shareholders.* [Reserved]

(d) *Relationship to section 6114(a) treaty-based return positions.* The statement required by paragraph (b) of this section will be considered disclosure for purposes of section 6114 and § 301.6114–1(a), but only if the statement is in the form required by paragraph (c) of this section. If the taxpayer fails to file the statement required by paragraph (b) of this section on or before the date prescribed in paragraph (b) of this section, the taxpayer will be subject to the penalties imposed by section 6712. See section 6712 and § 301.6712–1.

(e) *Examples.* The following examples illustrate the application of this section:

*Example 1.* B, an alien individual, is a resident of foreign country X, under X's internal law. Country X is a party to an income tax convention with the United States. B is also a resident of the United States under the Internal Revenue Code. B is considered to be a resident of country X under the convention. The convention does not specifically deal with characterization of foreign corporations as controlled foreign corporations or the taxability of United States shareholders on inclusions of subpart F income, but it provides, in an ''Other Income'' article similar to Article 21 of the 1981 draft of the United States Model Income Tax Convention (U.S. Model), that items of income of a resident of country X that are not specifically dealt with in the convention shall be taxable only in country X. B owns 80% of the one class of stock of foreign corporation R. The remaining 20% is owned by C, a United States citizen who is unrelated to B. In 1985, corporation R's only income is interest that is foreign personal holding company income under § 1.954A-2 of this chapter. Because the United States-X income tax convention does not deal with characterization of foreign corporations as controlled foreign corporations, United States internal income tax law applies.

Therefore, B and C are United States shareholders within the meaning of §1.951–1(g) of this chapter, corporation R is a controlled foreign corporation within the meaning of §1.957–1 of this chapter, and corporation R's income is included in C's income as subpart F income under §1.951–1 of this chapter. B may avoid current taxation on his share of the subpart F inclusion by filing as a nonresident (*i.e.*, by following the procedure in §301.7701(b)–7(b)).

*Example 2.* The facts are the same as in *Example 1,* except that B also earns United States source dividend income. The United States-X income tax convention provides that the rate of United States tax on United States source dividends paid to residents of country X shall not exceed 15 percent of the gross amount of the dividends. B's United States tax liability with respect to the dividends would be smaller if he were treated as a resident alien, subject to tax on a net basis (*i.e.*, after the allowance of deductions) than if he were treated as a nonresident alien. If, however, B chooses to file as a nonresident in order to claim treaty benefits with respect to his share of R's subpart F income, his overall United States tax liability, including the portion attributable to the dividends, must be determined as if he were a nonresident alien.

*Example 3.* C, a married alien individual with three children, is a resident of foreign country Y, under Y's internal law. Country Y is a party to an income tax convention with the United States. C is also a resident of the United States under the Internal Revenue Code. C is considered to be a resident of country Y under the convention. The convention specifically covers, among other items of income, personal services income, dividends and interest. C is sent by her country Y employer to work in the United States from January 1, 1985 until December 31, 1985. During 1985, C also earns United States source dividends and interest and incurs mortgage interest expenses on her personal residence. The United States-Y treaty provides that remuneration for personal services performed in the United States by a country Y resident is exempt from United States tax if, among other things, the individual performing such services is present in the United States for a period that is not in excess of 183 days. The treaty provides that the rate of United States tax on United States source dividends paid to residents of Y shall not exceed 15 percent of the gross amount of the dividends and it exempts residents of Y from United States tax on United States source interest. In filing her 1985 tax return, C may choose to file either as a resident alien without claiming any treaty benefits or as a nonresident alien if she desires to claim any treaty benefit. C files as a nonresident (*i.e.* by following the procedure described in §301.7701(b)–7(b)). Because C does not satisfy the requirements of the United States-Y treaty with regard to exempting personal services income from United States tax, C will be taxed on her personal services income at graduated rates under section 1 of the Code pursuant to section 871(b) of the Code. She will not be entitled to deduct her mortgage interest expenses or to claim more than one personal exemption because she is taxed as a nonresident alien under the Code by virtue of her decision to claim treaty benefits, and section 873 of the Code denies nonresidents the deduction for personal residence mortgage interest expense and generally limits them to only one personal exemption. C will be subject to a tax of 15 percent of the gross amount of her dividend income under section 871(a) of the Code as modified by the treaty, and she will be exempt from tax on her interest income. C is not entitled to file a joint return with her spouse even if he is a resident alien under the Code for 1985.

*Example 4.* The facts are the same as in *Example 3,* except that C does not choose to claim treaty benefits with respect to any items of income covered by the treaty (*i.e.*, she files as a resident). Therefore, she is taxed as a resident under the Code and pays tax at graduated rates on her personal services income, dividends, and interest. In addition, she is entitled to deduct her mortgage interest expenses and to take personal exemptions for her spouse and three children. C will be entitled to file a joint return with her spouse if he is a resident alien for 1985 or, if he is a nonresident alien, C and her spouse may elect to file a joint return pursuant to section 6013.

[T.D. 8411, 57 FR 15251, Apr. 27, 1992; 57 FR 28612, June 26, 1992, as amended by T.D. 8733, 62 FR 53387, Oct. 14, 1997]

### §301.7701(b)–8 Procedural rules.

(a) *Who must file*—(1) *Closer connection exception.* An alien individual who otherwise meets the substantial presence test must file a statement to explain the basis of the individual's claim that he or she is able to satisfy the closer connection exception described in §301.7701(b)–2.

(2) *Exempt individuals and individuals with a medical condition.* An alien individual must file a statement to explain the basis of the individual's claim that he or she is able to exclude days of presence in the United States because the individual—

(i) Is an exempt individual as described in §301.7701(b)–3(b)(3) (teacher/trainee) or (b)(4) (student);