



# Foreign Persons

## Rules relevant to chapters 3 and 4

A payee is subject to withholding only if it is a foreign person. A foreign person includes a nonresident alien individual, foreign corporation, foreign partnership, foreign trust, foreign estate, and any other person that is not a U.S. person. It also includes a foreign branch of a U.S. financial institution if the foreign branch is a qualified intermediary. In most cases, the U.S. branch of a foreign corporation or partnership is treated as a foreign person.

If an amount is both a withholdable payment and an amount subject to chapter 3 withholding and the withholding agent withholds under chapter 4, it may credit this amount against any tax due under chapter 3.

## Nonresident alien

A nonresident alien is an individual who is not a U.S. citizen or a resident alien. A resident of a foreign country under the residence article of an income tax treaty is a nonresident alien individual for purposes of withholding.

**Married to U.S. citizen or resident alien.** Nonresident alien individuals married to U.S. citizens or residents may choose to be treated as resident aliens for certain income tax purposes. However, these individuals are still subject to the chapter 3 withholding rules that apply to nonresident aliens for all income except wages. Wages paid to these individuals are subject to graduated withholding.

## U.S. person

The term "United States person" means:

- A citizen or resident of the United States,
- A partnership created or organized in the United States or under the law of the United States or of any State, or the District of Columbia,
- A corporation created or organized in the United States or under the law of the United States or of any State, or the District of Columbia,
- Any estate or trust other than a foreign estate or foreign trust. (See Internal Revenue Code section 7701(a)(31) for the definition of a foreign estate and a foreign trust.), or

- Any other person that is not a foreign person.

## U.S. citizen

The term "United States citizen" means:

- An individual born in the United States,
- An individual whose parent is a U.S. citizen,
- A former alien who has been naturalized as a U.S. citizen,
- An individual born in Puerto Rico,
- An individual born in Guam, or
- An individual born in the U.S. Virgin Islands.

## Resident alien

A resident alien is an individual that is not a citizen or national of the United States and who meets either the [green card test](#) or the [substantial presence test](#) for the calendar year.

In most cases, the days the alien is in the United States as a teacher, student, or trainee on an "F", "J", "M", or "Q" visa are not counted. This exception is for a limited period of time. For more information on resident and nonresident status, the tests for residence, and the exceptions to them, refer to [Publication 519, U.S. Tax Guide for Aliens](#).

**Note:** If your employee is late in notifying you that his or her status changed from nonresident alien to resident alien, you may have to make an adjustment to [Form 941](#) if that employee was exempt from withholding of social security and Medicare taxes as a nonresident alien. For more information on making adjustments, refer to Chapter 13 of [Publication 15, \(Circular E\), Employer's Tax Guide](#).

**Resident of a U.S. possession.** A bona fide resident of Puerto Rico, the U.S. Virgin Islands, Guam, the Commonwealth of the Northern Mariana Islands (CNMI) or American Samoa who is not a U.S. citizen or a U.S. national is treated as a nonresident alien for the withholding rules explained here. A bona fide resident of a possession is someone who:

- Meets the presence test,
- Does not have a tax home outside the possession, and
- Does not have a closer connection to the United States or to a foreign country than to the possession.

Section 937 of the Internal Revenue Code establishes the filing requirement for [Form 8898, Statement for Individuals Who Begin or End Bona Fide Residence in a U.S. Possession](#). This form reports each change of residency to or from a U.S. possession. The IRS is authorized to impose a \$1,000 penalty on any taxpayer who is liable to file this form, but who fails to file it.

For a detailed explanation of the U.S. possession residency rules and income sourcing rules, please refer to [Publication 570, Tax Guide for Individuals With Income From U.S. Possessions](#).

## Foreign corporations

A foreign corporation is one that does not fit the definition of a domestic corporation. A domestic corporation is one that was created or organized in the United States or under the laws of the United States, any of its states, or the District of Columbia.

**Guam or Northern Mariana Islands corporations.** A corporation created or organized in, or under the laws of, Guam is not considered a foreign corporation for the purpose of withholding tax for the tax year if:

- At all times during the tax year less than 25% in value of the corporation's stock is owned, directly or indirectly, by foreign persons, and
- At least 20% of the corporation's gross income is derived from sources within Guam or the CNMI for the 3-year period ending with the close of the preceding tax year of the corporation (or the period the corporation has been in existence, if less).

**Note:** The provisions discussed below under U.S. Virgin Islands and American Samoa Corporations will apply to Guam or CNMI corporations when an implementing agreement is in effect between the United States and that possession.

**U.S. Virgin Islands and American Samoa corporations.** A corporation created or organized in, or under the laws of, the U.S. Virgin Islands or American Samoa is not considered a foreign corporation for the purposes of withholding tax for the tax year if:

- At all times during the tax year less than 25% in value of the corporation's stock is owned, directly or indirectly, by foreign persons.
- At least 65% of the corporation's gross income is effectively connected with the conduct of a trade or business in the U.S. Virgin Islands, American Samoa, Guam, the CNMI, or the United States for the 3-year period ending with the close of the tax year of the corporation (or the period the corporation or any predecessor has been in existence, if less), and
- No substantial part of the income of the corporation is used, directly or indirectly, to satisfy obligations to a person who is not a bona fide resident of the U.S. Virgin Islands, American Samoa, Guam, the CNMI, or the United States.

## Foreign private foundation

A private foundation that was created or organized under the laws of a foreign country is a foreign private foundation. Gross investment income from sources within the United States paid to a qualified foreign private foundation is subject to withholding of a 4% rate (unless exempted by a treaty) rather than the ordinary statutory 30% rate.

## Other foreign organizations, associations, and charitable institutions

An organization may be exempt from income tax under section 501(a) of the Internal Revenue Code and chapter 4 withholding tax even if it was formed under foreign law. In most cases, you do not have to withhold tax on payments of income to these foreign tax-exempt organizations unless the IRS has determined that they are foreign private foundations. As a general rule, such foreign tax-exempt organizations should file [Form W-8 EXP](#) with the withholding agent in order to establish their status as a foreign tax-exempt organization.

Payments to these organizations, however, must be reported on [Form 1042-S](#) if the payment is subject to chapter 3 withholding, even though no tax is withheld.

You must withhold tax on the unrelated business income (as described in [Publication 598, Tax on Unrelated Business Income of Exempt Organizations](#)) of foreign tax-exempt organizations in the same way that you would withhold tax on similar income of nonexempt organizations when the organization does not provide you a [Form W-8 ECI](#) to certify that the income is effectively connected with a U.S. trade or business of the organization.


## U.S. branches of foreign persons

In most cases, a payment to a U.S. branch of a foreign person is a payment made to the foreign person. You may, however, treat payments to U.S. branches of foreign banks and foreign insurance companies that are subject to U.S. regulatory supervision as payments made to a U.S. person, if you and the U.S. branch have agreed to do so, and if their agreement is evidenced by a withholding certificate, [Form W-8 IMY, Certificate of Foreign Intermediary, Foreign Flow-Through Entity, or Certain U.S. Branches for United States Tax Withholding](#). For this purpose, a territory financial institution acting as an intermediary or that is a flow-through entity is treated as a U.S. branch.

## References/Related Topics

- [NRA Withholding](#)
- [Publication 15, \(Circular E\), Employer's Tax Guide](#)
- [Publication 515, Withholding of Tax on Nonresident Aliens and Foreign Entities](#)
- [Publication 519, U.S. Tax Guide for Aliens](#)
- [Publication 570, Tax Guide for Individuals With Income From U.S. Possessions](#)

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**Note:** This page contains one or more references to the Internal Revenue Code (IRC), Treasury Regulations, court cases, or other official tax guidance. References to these legal authorities are included for the convenience of those who would like to read the technical reference material. To access the applicable IRC sections, Treasury Regulations, or other official tax guidance, visit the [Tax Code, Regulations, and Official Guidance](#) page. To access any Tax Court case opinions issued after September 24, 1995, visit the [Opinions Search](#)  page of the United States Tax Court.

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