Leonard Larsen v. Commissioner, 23 T.C. 599 (1955)

A U.S. citizen's bona fide residency in a foreign country for purposes of the foreign earned income exclusion is determined by the intent and nature of their stay, considering whether they are a transient or a sojourner.

Summary

In *Leonard Larsen v. Commissioner*, the U.S. Tax Court addressed whether the taxpayer qualified for the foreign earned income exclusion under Section 116(a) of the 1939 Internal Revenue Code. The court examined when Larsen established bona fide residency in Argentina. The court held that Larsen became a resident when he formed the intention to be a permanent employee of the Argentine subsidiary, coupled with his physical presence in Argentina for an extended stay, even if he maintained a general intent to eventually return to the U.S. This decision clarified the factors used to determine residency for tax purposes, especially the importance of the taxpayer's intentions regarding the length and nature of their stay in a foreign country.

Facts

Leonard Larsen, a U.S. citizen, worked in Argentina. The crucial question was when his residency in Argentina began. In October 1947, he was informed he would become a permanent employee of an Argentine subsidiary. In December 1947, he returned to the United States and then returned to Argentina in February 1948 with his family. The IRS argued that Larsen was not a bona fide resident of Argentina for the entire year 1948, therefore his income was taxable. Larsen and his wife contended that he was an Argentine resident during the entire year 1948.

Procedural History

The case was brought before the U.S. Tax Court to determine if Larsen met the requirements for the foreign earned income exclusion for the year 1948. The court examined the facts, focusing on Larsen's intentions and the nature of his stay in Argentina, to determine when his residency commenced.

Issue(s)

1. Whether Larsen was a bona fide resident of Argentina for the entire taxable year of 1948, allowing him to claim the foreign earned income exclusion.

Holding

1. Yes, because the court found that Larsen formed the intent to be a permanent employee of the Argentine subsidiary in October 1947 and thus established bona fide residency. This intention, coupled with his physical presence in Argentina, satisfied the residency requirements for tax purposes.

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Court’s Reasoning

The court applied Section 116(a) of the 1939 Code, which provides a tax exemption for earned income from sources outside the United States if the individual is a bona fide resident of a foreign country for the entire taxable year. The court referenced regulations that outlined criteria for determining residency, similar to those used to determine whether an alien is a resident of the United States. The regulations defined the terms “transient” and “sojourner.” The court determined that Larsen was not a transient because his intention was to work in Argentina for an extended time. The court emphasized that the taxpayer’s intention regarding the length and nature of their stay, along with their physical presence in the foreign country, was critical. The court specifically found that the time Larsen was informed he would become a permanent employee constituted the beginning of his Argentine residency.

The court stated, “We are convinced from the evidence that in October 1947 he then formed an intention to be an Argentine resident. The intention plus his physical presence where he had a job for an extended stay is sufficient to meet the ‘bona fide resident’ requirements of section 116 (a) of the Code, and the corresponding regulations.”

Practical Implications

This case provides a guide for determining when U.S. citizens become residents of foreign countries for federal tax purposes, particularly in situations involving the foreign earned income exclusion. The decision highlights the importance of the taxpayer’s intent regarding the length and nature of their stay. Attorneys should advise clients on the documentation needed to demonstrate intent, such as employment contracts, lease agreements, and any evidence that supports an extended stay. This case emphasizes that even with an eventual intention to return to the U.S., the taxpayer’s actions and intentions in the foreign country are paramount in determining residency status. Later cases have followed Larsen’s interpretation of the regulations, affirming the use of similar tests to decide residency questions for tax purposes, specifically examining intent, and the nature of the stay.

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