Lemery v. Commissioner, 54 T. C. 480; 1970 U. S. Tax Ct. LEXIS 192 (U. S. Tax Court, March 12, 1970)

A nonresident alien's tax residency status is determined by the date of actual departure from the U. S. , not by an intention to leave.

Summary

Douglas J. Lemery, a Canadian citizen, sold stock in the U. S. in 1964, realizing a capital gain but did not report it on his Nonresident Alien Income Tax Return. The key issue was whether Lemery qualified as a nonresident alien under the U. S. -Canada tax treaty, which would exempt his capital gain from U. S. taxation. The Tax Court ruled that Lemery was a U. S. resident at the time of the stock sale because he had not yet departed the U. S. , despite his intention to leave. Consequently, his capital gain was taxable. However, the court found that Lemery was not liable for negligence penalties due to confusion caused by an outdated IRS ruling.

Facts

Douglas J. Lemery, a Canadian citizen, entered the U. S. in 1958 as a permanent resident. He purchased a home in Washington and enrolled his children in local schools. In 1964, Lemery sold stock in Code-A-Phone Electronics, Inc. , realizing a significant capital gain. He moved to Canada in June 1964 but did not report the gain on his U. S. Nonresident Alien Income Tax Return for the period January 1 to May 31, 1964, relying on an IRS ruling (O. D. 468) and the U. S. -Canada tax treaty.

Procedural History

The IRS issued a deficiency notice for 1964, asserting that Lemery was liable for tax on the capital gain and additional penalties for negligence. Lemery petitioned the U. S. Tax Court, arguing that he was exempt from U. S. tax under the treaty. The Tax Court held a trial and issued its opinion on March 12, 1970.

Issue(s)

1. Whether Lemery's capital gain from the sale of stock in 1964 was exempt from U. S. taxation under Article VIII of the U. S. -Canada Income Tax Convention?
2. Whether Lemery is liable for additions to the tax under section 6653(a) for negligence or intentional disregard of rules and regulations?

Holding

1. No, because Lemery was a U. S. resident at the time of the stock sale, not a nonresident alien as required by the treaty for exemption.
2. No, because the confusion caused by O. D. 468 precluded a finding of negligence or intentional disregard of rules and regulations.

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Court’s Reasoning

The court applied the legal rule from section 1. 871-5 of the Income Tax Regulations, which states that an alien retains U. S. residency until actually departing the country. Lemery’s actions, including purchasing a home and enrolling his children in school, demonstrated U. S. residency. The court found that O. D. 468, which Lemery relied on, was in direct conflict with the regulation and lacked the force of law. The court also considered the policy of consistent application of tax laws and the need to clarify residency status. The court quoted the regulation, stating, “An alien who has acquired residence in the United States retains his status as a resident until he abandons the same and actually departs from the United States. ” The court noted a dissenting opinion in a similar case, Friedman, but distinguished it due to different factual circumstances. The court concluded that the confusion caused by O. D. 468 precluded a finding of negligence under section 6653(a).

Practical Implications

This decision clarifies that nonresident alien status for tax purposes hinges on actual departure from the U. S. , not merely an intention to leave. Tax practitioners must advise clients to file appropriate returns and consider the timing of asset sales relative to departure dates. The ruling underscores the importance of current IRS guidance over outdated rulings. Subsequent cases, such as Verrier Friedman, have cited Lemery in distinguishing between intent and actual residency changes. This decision impacts how international taxpayers manage their U. S. tax obligations, particularly around the timing of significant financial transactions near their departure.

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