

Maximizing Tax Benefits for Nonresident Investors: The Essential Role of the ECI Election



The Hidden Default That Could Be Costing You Thousands

Nonresident investors earning rental income from U.S. properties may be subject to an important tax classification that often goes unnoticed. By default, the IRS classifies rental income as Fixed, Determinable, Annual, or Periodical (FDAP) income, subjecting it to a flat 30% withholding tax on gross income without allowing any deductions. This classification often leads to higher tax liabilities than necessary, especially for investors with significant property-related expenses.

The key to unlocking better tax treatment lies in an active choice: electing to treat rental income as Effectively Connected Income (ECI). This election is not automatic—it must be made deliberately to secure the benefits of taxation on net income, deductions for expenses, and lower effective tax rates.

What the ECI Election Can Do For You

By electing ECI treatment, nonresident investors can:

- **Deduct Property Expenses:** Include costs such as maintenance, depreciation, repairs, and mortgage interest to reduce taxable income.
- **Access Lower Tax Rates:** Shift from a flat 30% withholding on gross income to graduated tax rates for individuals or the 21% corporate tax rate for entities.
- **Utilize Losses:** Apply rental property losses to offset other U.S.-source income, further minimizing overall tax liability.

Example Savings

- A nonresident investor earns \$100,000 in rental income and has \$60,000 in expenses.
 - Under **FDAP**, they owe \$30,000 (30% of gross income).
 - Under **ECI**, they're taxed on \$40,000 net income. At an individual graduated rate, taxes could be as low as \$8,800—a savings of over \$21,000.

Why Timing and Accuracy Matter

The ECI election must be made by filing the appropriate forms, such as Form 1040-NR (for individuals) or Form 1120-F (for corporations), with a valid election statement. Missing deadlines or filing incorrectly can result in the loss of these benefits, leaving investors stuck with the default FDAP treatment.

Take Control of Your Tax Strategy

Don't let the IRS default dictate your tax liability. Contact **Gwayne Lai** or **Kevin Brown** from Anchin's International Tax Group, or your Anchin Relationship Partner today to ensure your U.S. rental income is treated as ECI. Our specialists will guide you through the election process, help you calculate potential savings, and ensure compliance – so you can keep more of what you earn.



GWAYNE LAI, CPA, MS
Partner —
International Services Group
gwayne.lai@anchin.com



KEVIN BROWN, EA, TEP
Principal —
Private Client Group
kevin.brown@anchin.com