

WHO HAS TO FILE A U.S. TAX RETURN? (And withholding requirement on alimony paid to a nonresident alien.)

Citizens of the U.S. and resident aliens must file and report all income from all sources, including sources outside of the U.S., if they meet certain threshold amounts. This income is taxed at graduated rates.

Nonresident aliens are generally taxed in the same manner as a U.S. citizen on all income that is “effectively connected” with the conduct of a trade or business in the U.S.

New for 2006: Generally, the requirement to file a return has been eliminated for nonresident aliens who earn wages effectively connected with a U.S. trade or business that are less than the amount of one personal exemption (\$3,400 for 2007).

A nonresident alien who is married to a U.S. citizen must use the tax rate schedule for married individuals filing separately unless the election to be treated as a resident is made, in which case a joint return is possible. Nonresident aliens who are unmarried must use the tax rate schedule for single individuals. The head of household tax rate schedule may not be used (Reg. §1.2-2(b)(6)).

If a nonresident alien is married to a U.S. citizen and does not elect to be treated as a resident, then any community-property income is NOT reported 50% each. Rather, each spouse reports what they individually earned.

If any U.S.-source income received by a nonresident alien is NOT effectively connected with a U.S. trade or business, then it will be taxed at a flat 30% rate. This may include fixed or determinable periodic income, capital gains and ALIMONY.

Unless there is a tax treaty with the country where a nonresident alien spouse or former spouse resides, the payor spouse, whether a U.S. citizen or resident alien, must withhold 30% for U.S. income taxes from the payment. This is true even when alimony is pursuant to a decree of a foreign country. The payor spouse is liable for the tax if he or she fails to collect it. The income tax liability cannot be avoided by paying alimony from a foreign bank account or from any other foreign source. Further, even if the foreign taxpayer pays the tax, the payor may still be liable for any interest, penalties or additions for failure to withhold. (IRC §1464.)

See IRS Publication 515 (Revised January 2006) “Withholding of Tax on Nonresident Aliens and Foreign Entities for Withholding in 2006,” page 36 for a list of countries NOT requiring withholding.

An annual return on Form 1042 is due from the payor on or before March 15 of each year in the Philadelphia office of the IRS. (IRC §871.)

As with most tax rules, these rules also are subject to change. Be advised to check with your friendly CPA when delving in this area.