



AVOIDING POTENTIAL PITFALLS OF U.S. INCOME TAX REPORTING REQUIREMENTS



By:

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About the Author:

Ms. Glendinning joined the firm in 1987 and has headed the International Tax Department since 1996. She has authored articles regarding various international tax issues and frequently gives presentations on U.S. income and estate taxation of foreign nationals doing business in the U.S.

Many foreign nationals dream of being able to live, work and raise their families in America. This dream comes true for quite a few of them. The enjoyment of the rights and privileges of living in America also comes with responsibilities. Not the least of these responsibilities is compliance with the reporting requirements of the U.S. income tax system for its residents.

One of the biggest mistakes that a new resident of the U.S. can make is to not be informed of how the tax reporting system applies to them and their specific circumstances. Many foreign nationals assume that the tax system in the U.S. is similar to that of their home country. This can be a very costly assumption to make, as each country has its own unique set of rules.

The first thing that needs to be determined is when the foreign national actually becomes a U.S. income tax resident. There are various rules that must be applied in order to determine when tax residency begins or ends, including visa status, dates entered or departed the country, number of days of physical presence in the calendar year and potential benefits under an income tax treaty between the U.S. and their home country. Making this determination can be quite a confusing and complicated task.

Once the foreign nationals have determined that they are a resident in the U.S. for purposes of income tax, they need to know what to report. Unlike some other countries, the U.S. tax laws require their tax residents to report their worldwide income. For instance, if foreign nationals receive interest income on their bank accounts in their home country, this interest income is subject to reporting on their U.S. income tax return. The same holds true for pensions, rental income, capital gains or any other type of income they receive from whatever source. This does not generally result in a double taxation due to the availability of tax credits and income tax treaty benefits. In addition, income that may not be subject to income tax in their home country could very well be subject to income tax in the U.S. Again, it is crucial to never assume that the tax laws of the countries are the same or similar.

Not all of the reporting requirements relate directly to the imposition of income tax. There are many disclosure requirements that apply to U.S. income tax residents, regardless of whether they have been residents their entire lives or have just recently become residents. This includes the disclosure of foreign (non-U.S.) bank accounts, closely-held companies and trusts. It also encompasses the receipt of a gift or inheritance from a foreign person. It is important to not confuse tax reporting with disclosure reporting. For example, the receipt of a gift or inheritance from a foreign person is not subject to income tax, but it is subject to disclosure. The principal of a foreign bank account is not taxable for income tax purposes, but the account details must be disclosed.

Each item subject to disclosure has its own form that must be completed and submitted to the proper authority by specific dates. The penalties for non-compliance or late compliance can be severe, i.e. , the penalty for not disclosing the existence of a foreign bank account could result in a penalty of one-half of the account balance or \$100,000, whichever is greater.

This article is not intended to alarm or discourage anyone from making the move to the U.S. Its intent is purely to inform. Many immigrants are unaware of the U.S. tax reporting and disclosure requirements. Unfortunately, not all U.S. tax professionals are fully aware of all the necessary disclosures. It is especially important that foreign nationals work with a tax professional that is knowledgeable with their specific issues and can help them avoid the potential pitfalls.

I would be happy to assist you with any of your questions. Please call (941-365-4617) or email (rglending@kbgrp.com).

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