



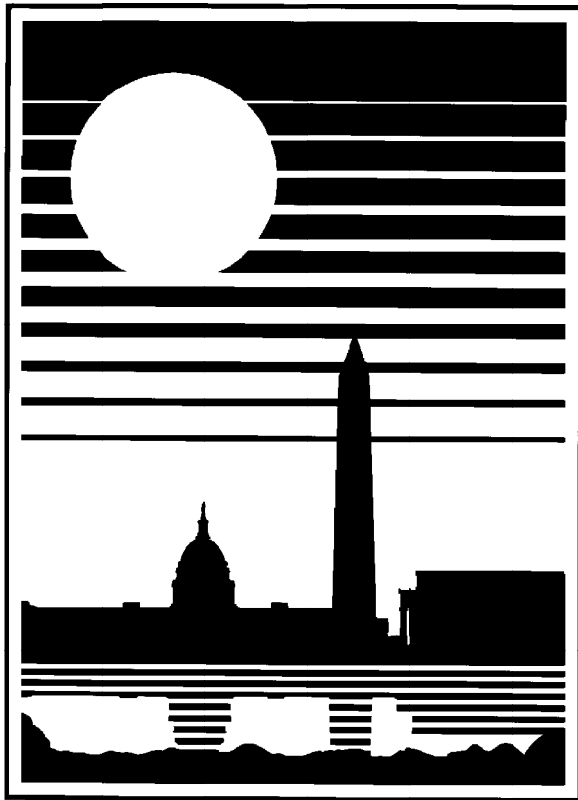
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Treasury

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Tax Guide for Individuals With Income From U.S. Possessions

For use in preparing
1996 Returns



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Important Change

Individual Taxpayer Identification Number (ITIN). The IRS will issue an ITIN to a nonresident or resident alien who does not have and is not eligible to get a social security number (SSN). To apply for an ITIN, Form W-7 must be filed with the IRS. It usually takes about 30 days to get an ITIN. The ITIN is entered wherever an SSN is requested on a tax return. If you are required to include another person's SSN on your return and that person does not have and cannot get an SSN, enter that person's ITIN.

An ITIN is for tax use only. It does not entitle you to social security benefits or change your employment or immigration status under U.S. law.

Important Reminder

Change of address. If you change your mailing address, be sure to notify the Internal Revenue Service using Form 8822, *Change of Address*. Mail it to the Internal Revenue Service Center for your old address (addresses for the Service Centers are on the back of the form).

Introduction

This publication will help individuals in U.S. possessions file their U.S. income tax returns. It also gives information and addresses for filing possession tax returns, if these returns are required. You should note that this publication is generally for use by U.S. citizens who have income from American Samoa, Guam, the Commonwealth of the Northern Mariana Islands, the Virgin Islands, or Puerto Rico.

An individual who is a bona fide resident of American Samoa may qualify to exclude income from sources in American Samoa, Guam, and the Commonwealth of the Northern Mariana Islands (CNMI) and income effectively connected with a trade or business in these possessions. This possession exclusion applies only to individuals.

For 1996, the exclusion applies only to bona fide residents of American Samoa. When implementing agreements between the United States and Guam and the CNMI go into effect, bona fide residents of each of these possessions may qualify for the exclusion. An

implementing agreement between the United States and Guam has been signed, but its effective date has been indefinitely postponed.

The publication also contains information for individuals who have income from the Virgin Islands and Puerto Rico. Those with income from sources in the Virgin Islands, who are not bona fide residents of the Virgin Islands on the last day of their tax year, must attach Form 8689, *Allocation of Individual Income Tax to the Virgin Islands*, to their Form 1040. They must also file a copy of their Form 1040 (with all attachments) with the Virgin Islands Bureau of Internal Revenue. For more information, see the discussion and the illustrated example of Form 8689, later in this publication.



If you need additional information on the U.S. taxation of individuals in U.S. possessions, write to:

Internal Revenue Service
Assistant Commissioner (International)
Attention: CP:IN:D:CS
950 L'Enfant Plaza South, S.W.
Washington, DC 20024

Useful Items

You may want to see:

Publication

- 54** Tax Guide for U.S. Citizens and Resident Aliens Abroad
- 514** Foreign Tax Credit for Individuals

Form (and Instructions)

- 1040** U.S. Individual Income Tax Return
- 1040-SS** U.S. Self-Employment Tax Return
- 1116** Foreign Tax Credit
- 4563** Exclusion of Income for Bona Fide Residents of American Samoa
- 5074** Allocation of Individual Income Tax to Guam or the Commonwealth of the Northern Mariana Islands (CNMI)
- 8689** Allocation of Individual Income Tax to the Virgin Islands

Ordering publications and forms. To order free U.S. income tax forms and publications, write to: Eastern Area Distribution Center, P.O. Box 25866, Richmond, VA 23286-8107. You can get any necessary possession tax forms at the appropriate possession tax office. The office addresses are given later. See also *How To Get More Information* near the end of this publication.

Problem Resolution Program (PRP). If you have a problem with the Internal Revenue Service that has not been resolved by your previous contacts with the Service, the Problem Resolution Office may be able to help you.

This office has been established to assist taxpayers who have problems with the Service that have not been resolved through normal channels. You can reach the PRP office by writing the Problem Resolution Officer in your IRS District or Service Center. If you are outside the United States, contact:

Internal Revenue Service
Assistant Commissioner (International)
Attention: CP:IN:D:PRO
950 L'Enfant Plaza South, S.W.
Washington, DC 20024

The Problem Resolution Office will ensure that your problem receives proper attention. Although this office cannot change the tax law or technical decisions, it can frequently clear up misunderstandings that resulted from previous contacts.

Possession Exclusion

For 1996, the possession exclusion applies only to bona fide residents of American Samoa.

Individuals in Guam, the CNMI, Puerto Rico, or the Virgin Islands are not eligible for the possession exclusion discussed here. The tax rules for each of these possessions are discussed later.

Qualifications

To qualify for the possession exclusion, you must be a **bona fide resident** of American Samoa for the entire tax year. For example, if your tax year is the calendar year, you must be a bona fide resident from January 1 through December 31. In addition to this time requirement, the following factors may be considered in determining bona fide residence:

- Your intent to be a resident of American Samoa, as shown by the circumstances,
- The establishment of a permanent home for you and members of your family in American Samoa for an indefinite period of time,
- The reason for and duration of your absences from American Samoa, and
- The type and duration of your job in American Samoa.

If you were not a bona fide resident of American Samoa for all of 1996, you cannot claim the possession exclusion. See *If You Do Not Qualify*, later for information on how to compute your tax liability in this case.

Sources of Income

If you qualify as a bona fide resident of American Samoa for 1996, you can exclude income from sources in American Samoa, Guam, or the CNMI and income effectively connected with your trade or business in these possessions.

General rules for determining the source of income are given below. For purposes of this discussion, the term **possession** means American Samoa, Guam, or the CNMI. If you

cannot clearly determine the source of your income, you should write to:

Internal Revenue Service
Assistant Commissioner (International)
Attention: CP:IN:D:CS
950 L'Enfant Plaza South, S.W.
Washington, DC 20024

Excludable income from sources within the possessions includes:

- 1) Wages, salaries, and other kinds of pay for personal services performed in the possessions. (But see *Exception*, below.)
- 2) Dividends received from possession sources, including those paid by:
 - a) U.S. corporations that do business in the possessions and elect the Puerto Rico and possession tax credit, and
 - b) Possession and foreign corporations that do business mainly in the possessions.
- 3) Interest on deposits paid by banks that do business mainly in the possessions, including interest paid on deposits with the possession branches of:
 - a) Domestic banks with commercial banking business in the possessions, and
 - b) Savings and loan associations chartered under federal or state laws.
- 4) Gains from the sale of securities, such as stock certificates, are from sources in the possessions if the seller's residence is in a possession and the sale is not attributable to an office or other fixed place of business maintained by the seller in the United States. However, see the *Caution*, below.

Income from sources outside the possessions includes:

- 1) Wages, salaries, and other kinds of pay for personal services performed outside the possessions. The source of the wages, salaries, etc., is the place where the services were performed even though payment is made in the possessions. (See *Exception*, below.)
- 2) Dividends paid by corporations not doing business in the possessions. Dividends paid by U.S. corporations doing business mainly in the United States are from U.S. sources. Dividends paid by foreign corporations not doing business mainly in the United States or in the possessions are from sources in foreign countries.
- 3) Interest paid on deposits with banks that do not carry on business in the possessions. Interest paid on bank deposits in the United States is interest from U.S. sources.

Exception. For the possession exclusion, the United States is the source of wages, salaries, etc., paid by the U.S. Government or any of its agencies to individuals who are its civilian or military employees.



CAUTION A U.S. person who becomes a resident of American Samoa, Guam, or the CNMI is subject to U.S. tax on U.S. source income, including gain from sales of certain U.S. assets, during the 10-year period beginning when the person becomes a resident. The U.S. person will be subject to U.S. tax on any gain from the disposition of U.S. property (including appreciated stock issued by a U.S. corporation) during this period.

Scholarships and fellowships. The source of a payment made as a scholarship or fellowship grant is generally the residence of the payer. The result is the same if payments are made by an agency acting on behalf of the payer.

Examples. The following examples illustrate the sources of income. Assume that corporations chartered in American Samoa (American Samoan corporations) do business only in American Samoa, and that the U.S. and foreign corporations do not carry on business in the possessions.

Example 1. Frank Harris, who is single, is an engineer who went to work in American Samoa for a private construction company on August 3, 1995, and lived there through 1996. He is a bona fide resident of American Samoa for 1996.

During 1996, he received wages of \$23,300 in American Samoa. He also received dividends of \$400 from U.S. corporations, dividends of \$100 from foreign corporations, and interest of \$1,300 from deposits in U.S. banks.

Gross income during the bona fide residence period Jan. 1, 1996, through Dec. 31, 1996

Samoan wages	\$23,300	
Nonpossession source income:		
Dividends (U.S.)	400	
Dividends (foreign)	100	
Interest (U.S.)	1,300	1,800
Total income		<u>\$25,100</u>

Frank's possession source income eligible for the exclusion is \$23,300. Because Frank's remaining income is less than \$2,550, he does not have to file a U.S. tax return for 1996. However, he must file a tax return in American Samoa. See *Filing Tax Returns*, later.

Example 2. Oliver Hunter was employed by a private employer in American Samoa from June 16, 1995, through December 31, 1996. He is a bona fide resident of American Samoa for 1996.

During 1996, he received wages of \$16,000, dividends of \$2,000 from U.S. corporations, a capital gain of \$4,000 from the sale of stock in the United States, and interest of \$500 from a bank in Guam.

Gross income during the bona fide residence period Jan. 1, 1996, through Dec. 31, 1996

Possession source income:		
Samoan wages	\$16,000	
Guam interest	500	
		\$16,500
Nonpossession source income:		
U.S. dividends	2,000	
Capital gain (U.S. source) ...	4,000	6,000
Total income		<u>\$22,500</u>

Oliver's possession source income of \$16,500 is eligible for the exclusion. Oliver must file a U.S. income tax return to report his U.S. source income. He must complete and attach Form 4563, *Exclusion of Income for Bona Fide Residents of American Samoa*, to his U.S. return to show his excluded income.

Deductions and Credits

You can neither deduct nor claim a credit for items connected to your excluded possession income that you exclude from gross income on your U.S. income tax return.

Items that do not apply to a particular type of income must be divided between your excluded income from possession sources and income from all other sources to find the amount you can deduct on your U.S. tax return. Examples of these items are medical expenses, real estate taxes, mortgage interest on your home, and charitable contributions.

Standard deduction. The standard deduction does not apply to a particular type of income. It must be divided between your excluded income and income from other sources. This division must be made before you can determine if you must file a U.S. tax return, because the minimum income level at which you must file a return is based, in part, on the standard deduction for your particular filing status.

Figuring the deduction. To divide an item between your excluded income and income from other sources, multiply it by the following fraction:

$$\frac{\text{Gross income from sources outside the possessions}}{\text{Total gross income from all sources (including excluded possession income)}}$$

Example. Barbara Jones, a U.S. citizen, is single, under 65, and a bona fide resident of American Samoa. During 1996, she received \$20,000 of income from Samoan sources and \$5,000 of income from sources outside the possessions. She does not itemize her deductions. Her allowable standard deduction for 1996 is figured as follows:

$$\frac{\$ 5,000}{\$25,000} \times \$4,000 \text{ (standard deduction)} = \$800$$

Barbara must file a U.S. income tax return because her gross income (\$5,000) is more than her allowable standard deduction plus her exemption (\$800 + \$2,550 = \$3,350). See *Filing Tax Returns*, later.

Foreign tax credit. If you must report possession source income on your U.S. tax return, you can claim a foreign tax credit, figured on Form 1116, *Foreign Tax Credit*, for income taxes paid in the possessions on that income. You cannot claim a foreign tax credit for taxes paid on excluded possession income.

If you have income, such as U.S. Government wages, that is not excludable, and you have income from possession sources that is excludable, you must figure the credit by reducing your foreign taxes paid or accrued by the taxes based on the excluded income. To find the amount of this reduction, use the following formula:

$$\frac{\text{Excluded income from possession sources less deductible expenses based on that income}}{\text{Total income subject to possession tax less deductible expenses based on that income}} \times \frac{\text{Tax paid or accrued to possessions}}{\text{Total income subject to possession tax less deductible expenses based on that income}} = \text{Reduction in foreign taxes}$$

See the example under *Foreign tax credit*, in the discussion *The Commonwealth of Puerto Rico*, later. For more information on foreign tax credit, get Publication 514, *Foreign Tax Credit for Individuals*.

Personal exemptions. Personal exemptions are allowed in full. They are not divided.

Moving expenses. If you are claiming expenses for a move to a U.S. possession from the United States, or from a U.S. possession to the United States, you should use Form 3903, *Moving Expenses*. This type of move is not considered a foreign move. Get Publication 521, *Moving Expenses*, for more information.

If You Do Not Qualify

If you do not qualify for the possession exclusion because you are not a bona fide resident of American Samoa (as explained earlier), or not a bona fide resident of American Samoa for the entire year, you should figure your tax liability in the usual manner. You should report all your taxable income, including income from foreign and possession sources, and claim all allowable exemptions, deductions, and credits, following the instructions for Form 1040.

You can take a credit against your U.S. tax liability if you paid income taxes to a foreign country or a possession and reported income from sources outside the United States on your U.S. tax return. The amount of foreign or possession income taxes paid that you can claim as a credit is figured on Form 1116, which should be attached to your Form 1040. For more information, see Publication 514.

Filing Tax Returns

If you can claim the possession exclusion, you may not have to file a U.S. income tax return.

If you were a bona fide resident of American Samoa for all of 1996, and all of your income is from sources in American Samoa, Guam, or the CNMI, or is effectively connected with your trade or business in these

possessions, you do not have to file a U.S. income tax return. You may have to file a return in American Samoa. For information and an address for the taxing authority in American Samoa, see the discussion under *American Samoa*, later.

If you qualify for the possession exclusion as a bona fide resident of American Samoa for 1996 and you have income from sources other than American Samoa, Guam, or the CNMI, you must file a U.S. income tax return if your gross income is at least the amount shown below for your filing status plus your allowable standard deduction from the computation discussed earlier under *Standard deduction*.

Filing status:	Gross income of at least:
Single	\$ 2,550
Married, filing jointly	5,100
Married, filing separately	2,550
Head of household	2,550
Qualifying widow(er)	2,550

If you do not qualify for the possession exclusion, you must generally file a U.S. income tax return if your gross income was at least the amount shown below.

Filing status:	Gross income of at least:
Single	\$ 6,550
Married, filing jointly	11,800
Married, filing separately	2,550
Head of household	8,450
Qualifying widow(er)	9,250

If you are age 65 or over, and you do not qualify for the possession exclusion, the minimum income levels for filing a return increase. For these amounts, see the instructions for Form 1040.

Some persons must file a tax return even though their gross income is less than the amount shown above for their filing status. For these situations, see the instructions for Form 1040.

Example. Regina Gray, a U.S. citizen, uses a calendar tax year. She was employed in American Samoa from July 2, 1995, to January 1, 1997. Her 1996 income consisted of her salary from her job plus interest of \$500 on deposits in a U.S. bank.

Regina does not have to file a U.S. income tax return for 1996 because she can claim the possession exclusion for 1996, and her U.S. income is below the amount that would cause her to have to file a U.S. tax return.

Regina filed both U.S. and Samoan income tax returns for 1995, and she will file only a Samoan tax return for 1996.

Dependents filing requirements. Generally, a person who receives unearned income, such as interest and dividends, has total income of more than \$650, and can be claimed as a dependent on another person's return, must file a return. For more information, see the instructions for Form 1040.

Form 4563. If you must file a U.S. income tax return and you qualify for the possession exclusion, claim the exclusion by attaching Form

4563, *Exclusion of Income for Bona Fide Residents of American Samoa*, to Form 1040. Form 4563 is not an income tax return. It is an information form that allows you to show that you qualified for the possession exclusion during the tax year. Form 4563 must be filed with your Form 1040 and cannot be filed by itself. There is an example of a filled-in Form 4563 at the end of this publication.

When and Where to File

If you file on a calendar year basis, the due date for filing your U.S. income tax return is April 15 following the end of your tax year. If you use a fiscal year (a year ending on the last day of a month other than December), the due date is the 15th day of the 4th month after the end of your fiscal year. If any due date falls on a Saturday, Sunday, or legal holiday, your tax return is due on the next business day.

Extensions of time to file. If you live outside the United States and Puerto Rico and have your main place of business or post of duty outside the United States and Puerto Rico on the regular due date of your return, you are automatically granted a 2-month extension to file your return. If you file on a calendar year basis, you have until June 15. This extension is also available if you are on military duty outside the United States and Puerto Rico. Your assigned tour of duty outside the United States and Puerto Rico must include the entire due date of your return.

If you use this automatic 2-month extension, you must attach a statement to your return showing that you qualify for it. You must pay interest on any unpaid tax from the due date (April 15 if you file a calendar year return) to the date you pay the tax.

Joint return. If you and your spouse file a joint return, only one of you needs to meet the qualifications discussed above to take advantage of the automatic extension to June 15 for filing your tax return.

If you file separate returns instead of a joint return, only the spouse who meets the qualifications can use the automatic extension.

Form 4868, Application for Automatic Extension of Time To File U.S. Individual Income Tax Return. You can get an automatic 4-month extension of time to file your tax return by filing Form 4868. This 4-month extension is not in addition to the automatic 2-month extension explained earlier. The 4 months and the 2 months both begin on April 15. You must file Form 4868 by the due date for filing your return, as extended by the 2-month automatic extension (usually June 15). Clearly note across the top of the form "Taxpayer Abroad".

In filling out Form 4868, you must make a tentative tax estimate for the year and you should pay in full any tax due with the application. If you do not pay the tax due, you will be charged interest on any tax not paid by the regular due date of your return, and you may be charged a penalty for the late payment.

Any payment you made with the application for extension should be entered on line 55 of Form 1040. You cannot ask the Internal Revenue Service to figure your tax if you use the extension of time to file.

Form 2688, Application for Additional Extension of Time To File U.S. Individual Income Tax Return. Further extensions of the time to file are granted only under very unusual circumstances. If you need additional time to file, apply for the extension either in a letter or by filing Form 2688. Extensions beyond the 4-month automatic extension are not granted as a matter of course. You must show reasonable cause.

Except in undue hardship cases, an application for extension on Form 2688 will not be accepted until you have taken advantage of the automatic 4-month extension using Form 4868.

TIP Federal tax returns mailed by taxpayers in foreign countries are filed on time if they bear an official postmark dated by midnight of the due date, including any extensions. The postmark can be foreign.

Where to file. If you have to file Form 1040 with the United States, file it with the Internal Revenue Service Center, Philadelphia, PA 19255-0002.

Self-Employment Tax

A U.S. citizen who owns and operates a business must pay self-employment tax on net self-employment earnings of \$400 or more. This rule applies whether or not the earnings are excludable from gross income (or whether or not a U.S. income tax return must be filed).

Your payments of self-employment tax contribute to your coverage under the social security system. Social security coverage provides you with old age, survivor, and disability benefits and hospital insurance.

The maximum amount of earnings subject to social security (old age, survivor, and disability insurance) tax is \$62,700 for 1996. The tax rate is 12.4%. All earnings are subject to Medicare (hospital insurance) tax. The tax rate is 2.9%.

Self-employment tax form. Unless one of the following special income tax rules applies, figure your self-employment tax on Schedule SE (Form 1040) and attach it to your U.S. income tax return.

If you are a resident of American Samoa, Guam, the CNMI, or the Virgin Islands who has net self-employment income, and you do not have to file Form 1040 with the United States, use Form 1040-SS, *U.S. Self-Employment Tax Return*, to figure your self-employment tax.

If you are a resident of Puerto Rico, file Form 1040-SS or Form 1040-PR, if appropriate.

These forms must be filed with the Internal Revenue Service Center, Philadelphia, PA 19255.

Self-employment tax deductions. You can claim a deduction in figuring your net earnings from self-employment. This deduction is allowed only in figuring self-employment tax. It is not an income tax deduction. This deduction is figured on Schedule SE or Form 1040-SS (1040-PR).

Also, you can take a deduction of one-half of your self-employment tax on line 25 of Form 1040 in figuring adjusted gross income. This is an income tax deduction only; it is not a deduction in figuring net earnings from self-employment subject to self-employment tax.

If you are a bona fide resident of American Samoa or Puerto Rico, and you exclude your self-employment income from gross income, you cannot take the deduction on line 25 of Form 1040. You cannot deduct items related to excluded income.

If you have self-employment income that is partially excluded, only the part of the deduction that is based on the nonexcluded income is allowed. This would happen if, for instance, you have two businesses, and only the income from one of them is excludable.

Figure the tax on the nonexcluded income by multiplying your total self-employment tax (from Schedule SE) by the following fraction:

$$\frac{\text{Self-employment income that is not excluded}}{\text{Total self-employment income (including excluded income)}}$$

The result is your self-employment tax on nonexcluded income. You can deduct one-half of this amount on line 25 of Form 1040.

Credit for Excess FICA Employee Tax Withheld

If you had more than one employer for 1996, and your total wages were over \$62,700, your employers may have withheld too much social security tax. If so, you can take a credit for the excess amount on line 56 of Form 1040.

If any one employer withheld more than \$3,887.40 of social security tax, you must ask your employer to refund the excess to you. You cannot claim it on your return.

If you do not file Form 1040, you can claim a refund of the excess amount withheld by filing Form 843, *Claim for Refund and Request for Abatement*. Residents of Puerto Rico, the Virgin Islands, American Samoa, Guam, and the CNMI should file Form 843 with the Internal Revenue Service Center, Philadelphia, PA 19255.

Double Taxation

A mutual agreement procedure exists to settle issues where there is an inconsistency between the tax treatment by the IRS and the taxing authorities of the following possessions:

American Samoa,
Guam,
Puerto Rico, and
the Virgin Islands.

These issues usually involve allocations of income, deductions, credits, or allowances

between related persons, determinations of residency, and determinations of the source of income and related expenses.

Send your written request for assistance under this procedure to the

Internal Revenue Service
Assistant Commissioner (International)
950 L'Enfant Plaza South, S.W.
Washington, DC 20024.

Your request must contain a statement that assistance is requested under the mutual agreement procedure with the possession. It must also contain all the facts and circumstances relating to your particular case. To avoid unnecessary delays, make sure you include all of the following information:

- 1) Your name, address, and social security number.
- 2) The name, address, and social security number of the related person in the possession (if one is involved).
- 3) The tax year(s) in question and the Internal Revenue Service Center where your return was filed.
- 4) If income tax is involved, the type of income, a description of the transaction, activities, or other pertinent circumstances, and the positions taken by you and the possession tax agency.
- 5) The amount of the item (income, deduction, or credit) involved and the amount of tax the possession assessed or proposed to assess.
- 6) A description of the control and business relationships between you and the related person in the possession, if that applies.
- 7) A statement of the status of your tax liability for the year(s) in question and, if it applies, the status of the tax liability of the related person in the possession.
- 8) A statement whether you or the related person, if one is involved, is entitled to any possession tax incentive or subsidy program benefits for the year(s) in question.
- 9) Copies of any correspondence received from the possession tax agency and copies of any material you provided to them.
- 10) Copy of the possession tax return(s) for the year(s) in question.
- 11) A statement whether a foreign tax credit was claimed on your federal tax return for all or part of the possession tax paid or accrued on the item in question.
- 12) A statement whether your federal return or the return of the related person, if there is one, was examined, or is being examined.
- 13) A separate statement that you consent to the disclosure to the designated possession tax official of any or all of the items of information set forth in, or enclosed with, the request for assistance under this procedure.

All statements must be signed and dated.

Credit or refund. In addition to the tax assistance request, if you seek a credit or refund of any overpayment of United States tax paid on the income in question, you should file a claim on Form 1040X, *Amended U.S. Individual Income Tax Return*. Indicate on the form that a request for assistance under the mutual agreement procedure with the possession has been filed. Attach a copy of the request to the form.

You should take whatever steps must be taken under the possession tax code to prevent the expiration of the statutory period for filing a claim for credit or refund of a possession tax.

Filing Requirements for Individuals in U.S. Possessions

Guam, the CNMI, American Samoa, the Virgin Islands, and Puerto Rico have their own independent tax departments. An individual who has income from sources in these possessions will probably have to file a tax return with one of the possessions' tax departments. It is possible that you may have to file two annual tax returns: one with the possession's tax department and the other with the U.S. Internal Revenue Service.

You should ask for forms and advice about the filing of possession tax returns from that possession's tax department and not the Internal Revenue Service. In some situations you may have to determine if you are a resident or a nonresident of a certain possession. Contact the tax department of that possession for advice about this point.

The following discussions cover the general rules for filing returns in Guam, the CNMI, American Samoa, the Virgin Islands, and Puerto Rico for 1996.

Guam

Guam has its own tax system based on the same tax laws and tax rates that apply in the United States.



Requests for advice about Guam residency and tax matters should be addressed to:

Guam Department of Revenue and
Taxation
P.O. Box 23607
GMF, GU 96921



Telephone number (671) 475-5000
Fax number (671) 472-2643

If you are a U.S. citizen who derives income from sources in Guam and the United States, you must file your income tax return as explained below with either Guam or the United States, but not both. You are relieved of any income tax liability to the jurisdiction with which you do not have to file. If you have to file a return, you must include income from

all sources (including the United States and Guam).



If you are a resident of Guam on the last day of your tax year, you should file your return with the:

Department of Revenue and Taxation
Government of Guam
P.O. Box 23607
GMF, GU 96921

Include any balance of tax due on income derived from all sources with your tax return.

Example. Gary Barker was a resident of Guam during the entire year of 1996. His income consisted of wages of \$20,000 paid by a private employer and dividends of \$4,000 from U.S. corporations that carry on business mainly in the United States.

He must file a 1996 income tax return with the Government of Guam. He reports his gross income of \$24,000 on the return.

If you are a resident of the United States on the last day of your tax year, you should file your return with the Internal Revenue Service Center, Philadelphia, PA 19255-0002. Include any balance of tax due on income derived from all sources with your tax return.

If you are neither a resident of Guam nor a resident of the United States at the end of your tax year, you should file with Guam if you are a citizen of Guam but not otherwise a citizen of the United States (born or naturalized in Guam). If you are a U.S. citizen or resident but not otherwise a citizen or resident of Guam, you should file with the United States.

Example. William Berry, a U.S. citizen, was employed by a private company in Guam from June 1 through December 31, 1996. He received a salary of \$20,000 during that period for his work in Guam, \$4,000 in dividends from U.S. corporations that carry on business mainly in the United States, and \$1,000 in interest from deposits in U.S. banks. William contacted the Guam Department of Revenue and Taxation and was advised that he was not a resident of Guam. He must file a U.S. tax return. On his U.S. tax return, he reports the \$4,000 of dividends, the \$1,000 of interest, and the \$20,000 Guam salary in addition to any income he had in 1996 before June 1.

Joint return. If you file a joint return, you should file it (and pay the tax) with the jurisdiction where the spouse who has the greater adjusted gross income would have to file (if you were filing separately). If the spouse with the greater adjusted gross income is a resident of Guam at the end of the tax year, file the joint return with Guam. If the spouse with the greater adjusted gross income is a resident of the United States at the end of the tax year, file the joint return with the United States. For this purpose, income is determined without regard to community property laws.

Example. Bill White, a U.S. citizen, was a resident of the United States, and his wife, a citizen of Guam, was a resident of Guam at the end of 1996. Bill's income consisted of a

\$25,000 salary as an engineer. His wife earned \$15,000 as a teacher in Guam. Mr. and Mrs. White filed a joint return. Because Bill has the greater adjusted gross income, they must file their return with the United States and report the entire \$40,000 on that return.

U.S. military employees. If you are a member of the U.S. Armed Forces stationed on Guam, you are not considered a resident of Guam and you must file your return with the United States. However, if you are a member of the military and a citizen of Guam, or if you are a civilian employee of the military, you are subject to the same rules described in the previous paragraphs.

Income taxes withheld and estimated tax payments are taken into account in determining if there is tax due or an overpayment, whether or not the withholdings or payments were actually received by the jurisdiction with which the return must be filed. Any liability for underpayment of estimated tax is payable to the jurisdiction where you file your return for the tax year.

Payment of estimated tax. If you have to pay estimated tax, make your payment to the jurisdiction (United States or Guam) where you would file your income tax return if your tax year were to end on the date your estimated tax payment is first due. Generally, you should make your quarterly payments of estimated tax with the jurisdiction where you made your original estimated tax payment. However, see *Early payment of estimated tax*, below.

If you make a joint payment of estimated tax, make your payment with the jurisdiction where the spouse who has the greater estimated adjusted gross income would have to pay (if a separate payment were made). For this purpose, income is determined without regard to community property laws.

Example. Bill West is single and files his return on a calendar-year basis. He is a resident of the United States at the time that he must make his first payment of estimated income tax for the year. Since Bill does not expect to be a resident of Guam at the end of the year, he pays his estimated tax to the United States by April 15. Later in the year, however, Bill becomes a resident of Guam and receives income from Guam sources that causes him to refigure his estimated tax payments. The quarterly estimated tax payments must be made to the United States because he was a U.S. resident when his first payment of estimated tax was due. Because Bill is a resident of Guam at the end of his tax year, he must file his income tax return with Guam. On that return, he claims credit for the estimated tax payments made to the United States.

Early payment of estimated tax. If you make your first payment of estimated tax early and you do not send it to the jurisdiction to which you would have sent it if you had not made it early, make all later payments to the other jurisdiction.

Example. Peg Post is single and files her return on a calendar year basis. On March 1, Peg was a resident of the United States and made an early first payment of estimated income tax to the United States. Before the date Peg would otherwise have to make her first payment of estimated tax (April 15), she becomes a resident of Guam for the rest of the year. Peg must make the rest of her installment payments of estimated tax to Guam because she is a resident of Guam on the date that her first payment of estimated tax is otherwise due. At the end of the year, Peg will file her tax return with Guam and claim credit for all estimated tax installments on that return.

Estimated tax form. If your estimated income tax obligation is to the United States, use Form 1040-ES to figure your estimated tax, including self-employment tax. Use the payment vouchers for your payments.

If your estimated income tax obligation is to Guam, use their forms to figure your estimated income tax and make your payments. You will have to separately figure your estimated self-employment tax (you can use Form 1040-ES) and make payments with the payment vouchers to the address given in the Form 1040-ES instructions.

Information return. If your adjusted gross income from all sources is at least \$50,000, your gross income consists of at least \$5,000 from sources in Guam, and you file a U.S. income tax return, attach Form 5074, *Allocation of Individual Income Tax to Guam or the Commonwealth of the Northern Mariana Islands (CNMI)*, to Form 1040. You can get Form 5074 from most Internal Revenue Service offices. If you need further information on Form 5074, write to:

Internal Revenue Service
Assistant Commissioner (International)
Attention: CP:IN:D:CS
950 L'Enfant Plaza South, S.W.
Washington, DC 20024

Note: Guam and the United States have entered into an implementing agreement. **The effective date of the agreement, however, has been indefinitely postponed.** Under the agreement, Guam may enact its own laws for taxing residents of Guam as well as for taxing income sourced in Guam (or income effectively connected with a trade or business in Guam) and paid to a nonresident. Individuals who are bona fide residents of Guam and have income sourced outside Guam, the CNMI, or American Samoa may have to file a U.S. tax return. Individuals who are bona fide residents of Guam and have income sourced in any of the three possessions may be able to treat that income as exempt from U.S. income tax under the possession exclusion rules.

Double taxation. A mutual agreement procedure exists to settle cases of double taxation between the United States and Guam. See *Double Taxation*, earlier under *Filing Tax Returns*.

The Commonwealth of the Northern Mariana Islands

The Commonwealth of the Northern Mariana Islands (CNMI) has its own tax system based partly on the same tax laws and tax rates that apply to the United States and partly on local taxes imposed by the CNMI government.



Requests for advice about CNMI residency and tax matters should be addressed to:

Division of Revenue and Taxation
Commonwealth of the Northern
Mariana Islands
P. O. Box 5234, CHR8
Saipan, MP 96950

If you are a U.S. citizen who derives income from CNMI and United States sources, you must file your income tax return with either the CNMI or the United States as explained below. Do not file with both. You are relieved of any income tax liability to the jurisdiction with which you do not have to file. If you must file a return, be sure to include income from all sources (including the United States and the CNMI).

If you are a resident of the CNMI on the last day of your tax year, you should file your return with the Division of Revenue and Taxation at the address above. Include any balance of tax due on income derived from all sources with your tax return.

If you are a resident of the United States on the last day of your tax year, you should file your return with the Internal Revenue Service Center, Philadelphia, PA 19255-0002. Include any balance of tax due on income derived from all sources with your tax return.

If you are neither a resident of the CNMI nor a resident of the United States at the end of your tax year, but you are a citizen of the CNMI, you should file with the Division of Revenue and Taxation. File with the Internal Revenue Service Center, Philadelphia, PA 19255-0002, if you are a citizen of the United States.

Joint return. If you file a joint return, you should file it (and pay the tax) with the jurisdiction where the spouse who has the greater adjusted gross income would have to file (if you were filing separately). If the spouse with the greater adjusted gross income is a resident of the CNMI at the end of the tax year, file the joint return with the CNMI. If the spouse with the greater adjusted gross income is a resident of the United States at the end of the tax year, file the joint return with the United States. For this purpose, income is determined without regard to community property laws.

Payment of estimated tax. If you must pay estimated tax, make your payment to the jurisdiction (United States or the CNMI) where you would file your income tax return if your tax

year were to end on the date your first payment of estimated tax is due. Generally, you should make your quarterly payments of estimated tax with the jurisdiction where you made your first payment of estimated tax. However, see *Early payment of estimated tax*, below.

If you make a joint payment of estimated tax, make the payment to the jurisdiction where the spouse who has the greater estimated adjusted gross income would have to file (if a separate declaration were filed). For this purpose, income is determined without regard to community property laws.

Early payment of estimated tax. If you make your first payment of estimated tax early and the jurisdiction to which you make it is not the one to which it should have been made if you had not made it early you must make all later payments to the jurisdiction to which the first payment should have been made if you had not made it early.

Estimated tax form. If your estimated income tax obligation is to the United States, use Form 1040-ES to figure your estimated tax, including self-employment tax. Use the payment vouchers for your payments.

If your estimated income tax obligation is to the CNMI, use their forms to figure your estimated income tax and make your payments. You will have to separately figure your estimated self-employment tax (you can use Form 1040-ES) and make payments with the payment vouchers to the address given in the Form 1040-ES instructions.

Income taxes withheld and estimated tax payments are generally taken into account in determining if there is tax due or an overpayment, whether or not the withholdings or payments were actually received by the jurisdiction with which the return must be filed. Any liability for underpayment of estimated tax is payable to the jurisdiction where you file your return for the tax year.

Information return. If your adjusted gross income from all sources is at least \$50,000, your gross income consists of at least \$5,000 from sources in the CNMI, and you file a U.S. income tax return, attach Form 5074, *Allocation of Individual Income Tax to Guam or the Commonwealth of the Northern Mariana Islands (CNMI)*, to Form 1040. You can get Form 5074 from most Internal Revenue Service offices. If you need further information on Form 5074, write to:

Internal Revenue Service
Assistant Commissioner (International)
Attention: CP:IN:D:CS
950 L'Enfant Plaza South, S.W.
Washington, DC 20024

Note: When the CNMI and the United States enter into an implementing agreement, the CNMI may enact its own laws for taxing residents of the CNMI as well as for taxing income sourced in the CNMI (or income effectively connected with a trade or business in

the CNMI) and paid to a nonresident. Individuals who are bona fide residents of the CNMI and have income sourced outside the CNMI, Guam, or American Samoa may have to file a U.S. tax return. Individuals who are bona fide residents of the CNMI and have income sourced in any of the three possessions may be able to exclude that income under the possession exclusion rules when an implementing agreement is in effect.

American Samoa

American Samoa has its own separate and independent tax system. Although its tax laws are modeled on the U.S. Internal Revenue Code, there are certain differences.



Requests for advice about matters connected with Samoan taxation should be sent to:

Tax Division
Government of American Samoa
Pago Pago, American Samoa 96799

Residents of American Samoa. If you are a U.S. citizen and a resident of American Samoa, you must report your gross income from worldwide sources on your Samoan tax return. If you report non-Samoan source income on your Samoan tax return, you can claim a credit against your Samoan tax liability for income taxes paid on that income to the United States, a foreign country, or another possession.

If you are a resident of American Samoa for part of the tax year and you then leave American Samoa, you must file a tax return with American Samoa for the part of the year you were present in American Samoa.

Bona fide residents of American Samoa include military personnel whose official home of record is American Samoa.

Nonresidents of American Samoa. If you are a nonresident of American Samoa, you should report only income from Samoan sources on your Samoan tax return. U.S. citizens residing in American Samoa are considered residents of American Samoa for income tax purposes.

U.S. Government employees. If you are employed in American Samoa by either the U.S. Government or any of its agencies, or by the Government of American Samoa, you are subject to tax by American Samoa on your pay from either government. Whether you are subject to tax by American Samoa on your non-Samoan source income depends on your status as a resident or nonresident.

Wages and salaries paid by the Governments of the United States and American Samoa to U.S. citizens are also subject to U.S. federal income tax. These payments are not excludable under the possession exclusion.

If you report government wages on both your U.S. and Samoan tax returns, you can take a credit on your U.S. tax return for income taxes paid or accrued to American Samoa. You should figure that credit on Form 1116,

and attach that form to your U.S. tax return, Form 1040. Show your wages paid for services performed in American Samoa on Form 1116 as income from sources in a possession.

Estimated tax. If your estimated income tax obligation is to the United States, use Form 1040-ES to figure your estimated tax, including self-employment tax. Use the payment vouchers for your payments.

Double taxation. A mutual agreement procedure exists to settle cases of double taxation between the United States and American Samoa. See *Double Taxation*, earlier under *Filing Tax Returns*.

The Virgin Islands

An important factor in Virgin Islands taxation is whether, on the last day of the tax year, you are a bona fide resident of the Virgin Islands and not a visitor or tourist. If you are a temporary worker on the last day of the tax year, you may or may not be a bona fide resident of the Virgin Islands. You should contact the Virgin Islands Bureau of Internal Revenue for more information.

If you are a bona fide resident of the Virgin Islands on the last day of the tax year, you must file your annual tax return on Form 1040 with the Government of the Virgin Islands and pay the entire tax due to the Virgin Islands. You do not have to file with the IRS for any tax year in which you are a bona fide resident of the Virgin Islands on the last day of the year, provided you report and pay tax on your income from all sources to the Virgin Islands and identify the source(s) of the income on the return. If you have non-Virgin Islands source income, you must also file Virgin Islands Form 1040 INFO (Non-Virgin Islands Source Income of Virgin Islands Residents) with the Virgin Islands Bureau of Internal Revenue.



You can get this form by contacting:

Virgin Islands Bureau of Internal Revenue
9601 Estate Thomas
Charlotte Amalie
St. Thomas, U.S. Virgin Islands 00802



Telephone number (809) 774-5865
Fax number (809) 776-4037

Example. Mr. and Mrs. Maple left the United States on June 15, 1996, and arrived in the Virgin Islands on the same day. They qualified as bona fide residents of the Virgin Islands on the last day of their tax year, December 31, 1996.

Mr. and Mrs. Maple file their 1996 income tax return with the Government of the Virgin Islands along with a Form 1040 INFO. The Maples report their worldwide income and pay the entire tax for the year to the Virgin Islands. Even though they lived in the United States part of the year, their income tax obligations for that year are completely satisfied by filing

their return with, and paying their tax to, the Virgin Islands Bureau of Internal Revenue.

Non-Virgin Islands resident with Virgin Islands income. If you are a U.S. citizen or resident alien and you have income from sources in the Virgin Islands or income effectively connected with the conduct of a trade or business in the Virgin Islands, and you are not a bona fide resident of the Virgin Islands on the last day of your tax year, you must file identical tax returns with the United States and the Virgin Islands. You do this by filing the original return with the United States and filing a copy of the U.S. return (including all attachments, forms, and schedules) with the Virgin Islands Bureau of Internal Revenue by the due date for filing Form 1040.

The amount of tax you must pay to the Virgin Islands is figured by multiplying the total tax on your U.S. return (after certain adjustments) by a decimal. This decimal is found by dividing your adjusted gross income from the Virgin Islands by your worldwide adjusted gross income (from your U.S. return). Form 8689, *Allocation of Individual Income Tax to the Virgin Islands*, is used for this computation. You must complete this form and attach it to each copy of your return. You should pay any tax due to the Virgin Islands when you file your return with the Virgin Islands Bureau of Internal Revenue. You receive credit for taxes paid to the Virgin Islands by including the amount on line 30, Form 8689, in the total on Form 1040, line 58. On the dotted line next to line 58, write "Form 8689" and show the amount.

Do not enter the amount from Form 8689, line 34 on Form 1040.

See the illustrated example at the end of this publication.

Where to file. If you are not a bona fide resident of the Virgin Islands but you have income from the Virgin Islands, you must file Form 1040 and all attachments with the Internal Revenue Service Center, Philadelphia, PA 19255-0002, and with the Virgin Islands Bureau of Internal Revenue.



If you are a bona fide resident of the Virgin Islands you should file your return with:

Virgin Islands Bureau of Internal Revenue
9601 Estate Thomas
Charlotte Amalie
St. Thomas, U.S. Virgin Islands 00802

Contact that office for information about filing your Virgin Islands tax return.

Extensions of time to file. You can get an automatic 4-month extension of time to file your tax return by filing Form 4868, *Application for Automatic Extension of Time To File U.S. Individual Income Tax Return*. Bona fide residents of the Virgin Islands must file this form with the Virgin Islands Bureau of Internal Revenue. Non-Virgin Islands residents should file separate Forms 4868 with the IRS and the Virgin Islands Bureau of Internal Revenue and

make any payments due to the respective jurisdictions. However, the Virgin Islands Bureau of Internal Revenue will honor an extension request that was timely filed with the IRS.

If you need more time after filing Form 4868, file Form 2688, *Application for Additional Extension of Time To File U.S. Individual Income Tax Return*. For more information, see the Form 2688 instructions.

Double taxation. A mutual agreement procedure exists to settle cases of double taxation between the United States and the Virgin Islands. See *Double Taxation*, earlier under *Filing Tax Returns*.

The Commonwealth of Puerto Rico

The Commonwealth of Puerto Rico has its own separate and independent tax system. While it is modeled after the U.S. system, there are variations in law and tax rates. If you are a U.S. citizen who derives income from Puerto Rican sources, you will be liable for payment of Puerto Rican taxes. You may also be liable for filing a U.S. tax return.



Requests for information about the filing of Puerto Rican tax returns should be addressed to:

Department of the Treasury
Bureau of Income Tax
Consulting and Legislation Office
P.O. Box 2501
San Juan, Puerto Rico 00902-2501



Telephone number (809) 723-7085. To obtain Puerto Rican tax forms, contact the Planning and Research Office at the above address. The telephone number is (809) 725-8835.

Residents of Puerto Rico. If you are a U.S. citizen and also a resident of the Commonwealth of Puerto Rico for the entire tax year, you are generally liable for the payment of tax on your income from worldwide sources to Puerto Rico. Any wages and the cost-of-living allowance paid to you by the U.S. Government for working in Puerto Rico are subject to Puerto Rican tax. Advice about possible tax benefits under the Puerto Rican investment incentive programs is available from the Puerto Rican tax authorities. If you report U.S. source income on your Puerto Rican tax return, you can claim a credit against your Puerto Rican tax, up to the amount allowable, for income taxes paid to the United States.

Nonresidents of Puerto Rico. If you are a U.S. citizen and are not a resident of the Commonwealth of Puerto Rico, you are liable for the payment of tax to Puerto Rico only on your income from Puerto Rican sources. Wages that you earn for services performed in Puerto Rico for the U.S. Government or for private employers is income from Puerto Rican sources.

U.S. taxation. As a U.S. citizen, you are liable for the payment of U.S. federal income tax on your gross income from worldwide sources, no matter where your residence may be. However, a special rule applies if you are a bona fide resident of Puerto Rico for an entire tax year, or have been a bona fide resident of Puerto Rico for at least 2 years and later change your residence from Puerto Rico during a tax year.

Income you receive from Puerto Rican sources during your residence in Puerto Rico is exempt from U.S. tax. This includes income for the period of Puerto Rican residence in the year you change your residence from Puerto Rico if you resided there at least 2 years before the change. However, income you receive for services performed in Puerto Rico as an employee of the United States must be reported on your U.S. income tax return.

Deductions and credits. Deductions and credits that apply to your exempt Puerto Rican income are not allowable on your federal income tax return.

Deductions that do not specifically apply to any particular type of income must be divided between your income from Puerto Rican sources and income from all other sources to find the part that you can deduct on your U.S. tax return. Examples of deductions that do not specifically apply to a particular type of income are alimony payments, the standard deduction, and certain itemized deductions (such as medical expenses, charitable contributions, and real estate taxes and mortgage interest on your home).

To find the part of a deduction that is allowable, multiply the deduction by a fraction. The numerator of the fraction is your gross income from sources outside Puerto Rico, and the denominator is your total gross income from all sources including your exempt income from sources in Puerto Rico.

Example. You and your spouse are both under 65 and U.S. citizens who are bona fide residents of Puerto Rico for the entire year. You file a joint income tax return. During 1996, you earned \$15,000 from Puerto Rican sources and your spouse earned \$25,000 from the U.S. Government. You have \$16,000 of itemized deductions that do not apply to any specific type of income. These are medical expenses (doctor's fees) of \$4,000, real estate taxes of \$5,000, home mortgage interest of \$6,000, and charitable contributions of \$1,000 (cash contributions). You determine the amount of each deduction that you can claim on your Schedule A, Form 1040, by multiplying the deduction by the following fraction:

$$\frac{\text{Gross income subject to U.S. tax}}{\text{Gross income from all sources (including exempt Puerto Rican income)}}$$

SCHEDULE A—Itemized deductions should be modified as shown below:

Medical Expenses (doctor's fees)

$$\frac{\$25,000}{\$40,000} \times \$4,000 = \$2,500 \text{ (enter on line 1 of Schedule A)}$$

Real Estate Taxes

$$\frac{\$25,000}{\$40,000} \times \$5,000 = \$3,125 \text{ (enter on line 6 of Schedule A)}$$

Home Mortgage Interest

$$\frac{\$25,000}{\$40,000} \times \$6,000 = \$3,750 \text{ (enter on line 10 or 11 of Schedule A)}$$

Charitable Contributions (cash contributions)

$$\frac{\$25,000}{\$40,000} \times \$1,000 = \$625 \text{ (enter on line 15 of Schedule A)}$$

Enter on Schedule A, Form 1040, only the allowable portion of each deduction.

Standard deduction. The standard deduction does not apply to any specific type of income. The part of the standard deduction that is due to exempt Puerto Rican income cannot be claimed on your U.S. tax return. The computation is the same as for itemized deductions that are not related to any specific type of income (discussed above). Your standard deduction amount (see line 34 of Form 1040) is multiplied by a fraction, the numerator of which is gross income subject to U.S. income tax, and the denominator of which is gross income from all sources (including exempt Puerto Rican income).

This computation must be made before you can determine if you must file a U.S. tax return, because the minimum income level at which you must file a return is based, in part, on the standard deduction for your particular filing status.

Example. James and Joan Brown, both under 65, are U.S. citizens and bona fide residents of Puerto Rico. They file a joint income tax return. During 1996, they received \$15,000 of income from Puerto Rican sources and \$8,000 of income from sources outside Puerto Rico. They do not itemize their deductions. Their allowable standard deduction for 1996 is figured as follows:

$$\frac{\$8,000}{\$23,000} \times \$6,700 \text{ (standard deduction)} = \$2,330$$

The Browns must file a U.S. income tax return because their gross income (\$8,000) is more than their allowable standard deduction plus their exemptions (\$2,330 + \$5,000 = \$7,330).

The Browns should enter the allowable standard deduction amount as computed above (\$2,330) on line 34 of Form 1040 and they should write the following above it: "Standard deduction modified due to exempt income under section 933."

Personal exemptions are allowed in full and need not be divided.

Foreign tax credit. If you are a U.S. citizen and are not a bona fide resident of Puerto Rico for the entire tax year (or not a bona fide resident for at least 2 years who changes your residence from Puerto Rico in a tax year), you must report on your U.S. tax return all of your Puerto Rican income as well as all other income from worldwide sources. If you must report Puerto Rican income on your U.S. tax return, you can claim a foreign tax credit, figured on Form 1116, for income taxes paid to Puerto

Rico on that income. You cannot claim a foreign tax credit for taxes paid on exempt income from Puerto Rico.

If you have income from Puerto Rican sources, such as U.S. Government wages, that is not excludable, and you have income from Puerto Rican sources that is excludable, you must figure the credit by reducing your foreign taxes paid or accrued by the taxes based on the exempt income. To find the amount of this reduction, use the following formula:

$$\frac{\text{Exempt income from P.R. sources less deductible expenses based on that income}}{\text{Total income subject to Puerto Rican tax less deductible expenses based on that income}} \times \frac{\text{Tax paid or accrued to Puerto Rico}}{\text{Reduction in foreign taxes}}$$

Example. This example illustrates the taxation of U.S. citizens who have been bona fide residents of Puerto Rico for their entire tax year.

John and Mary Reddy, who were bona fide residents of Puerto Rico during the entire year of 1996, had the following income and expenses in that year:

John:

- \$25,000 wages as an employee of the U.S. Government working in Puerto Rico.
- \$200 dividend from a Puerto Rican corporation that does business in Puerto Rico.
- \$400 dividend from a United Kingdom corporation that does business in the United Kingdom.
- \$600 dividend from a U.S. corporation that does business in the United States.

Mary:

- \$15,000 wages from a Puerto Rican corporation for services performed in Puerto Rico.

John and Mary file a joint tax return. The following table shows their exempt and taxable income for U.S. federal income tax purposes.

	Taxable	Exempt
John's wages	\$25,000	
(U.S. Gov't. wages are not exempt)		
Mary's wages		\$15,000
P.R. corporation dividend		200
(Puerto Rican source income is exempt)		
U.K. corporation dividend	400	
(Income from sources outside Puerto Rico is taxable)		
U.S. corporation dividend	600	
Totals	<u>\$26,000</u>	<u>\$15,200</u>

John and Mary must file 1996 income tax returns with both Puerto Rico and the United States. They have gross income of \$26,000 for U.S. tax purposes. They paid taxes to Puerto Rico of \$5,000. The foreign tax credit is figured on Form 1116, which must be attached to their U.S. tax return, Form 1040. Foreign taxes paid are reduced by taxes paid on exempt income as follows:

$$\frac{\$15,200}{\$41,200} \times \$5,000 = \$1,845$$

\$1,845 is the amount of foreign taxes based on exempt income. This amount goes on

Form 1116, line 12 in the computation of John and Mary's allowable foreign tax credit.

Earned income credit. Even if you maintain a household in Puerto Rico that is your principal home and the home of your qualifying child, you cannot claim the earned income credit on your U.S. tax return. This credit is available only if you maintain the household in the United States or you are serving on extended active duty in the Armed Forces of the United States.

Estimated tax. If your estimated income tax obligation is to the United States, use Form 1040-ES to figure your estimated tax, including self-employment tax. Use the payment vouchers for your payments.

Double taxation. A mutual agreement procedure exists to settle cases of double taxation between the United States and the Commonwealth of Puerto Rico. See *Double Taxation*, earlier under *Filing Tax Returns*.

How To Get More Information



You can get help from the IRS in several ways.

Free publications and forms. To order free publications and forms, call 1-800-TAX-FORM (1-800-829-3676). You can also write to the IRS Forms Distribution Center nearest you. Check your income tax package for the address. Your local library or post office also may have the items you need.

For a list of free tax publications, order Publication 910, *Guide to Free Tax Services*. It also contains an index of tax topics and related publications and describes other free tax information services available from IRS, including tax education and assistance programs.

If you have access to a personal computer and modem, you also can get many forms and publications electronically. See *Quick and Easy Access to Tax Help and Forms* in your income tax package for details. If space permitted, this information is at the end of this publication.

Tax questions. You can call the IRS with your tax questions. Check your income tax package or telephone book for the local number, or you can call 1-800-829-1040.

TTY/TDD equipment. If you have access to TTY/TDD equipment, you can call 1-800-829-4059 to ask tax questions or to order forms and publications. See your income tax package for the hours of operation.

Illustrated Example of Form 4563

This example, illustrated on the filled-in Form 4563, shows how much income is excludable on John Black's 1996 tax return.

- 1) John, who is single and a U.S. citizen, was employed in American Samoa by the Samoa Products Co., a private Samoan corporation during all of 1996. He began to reside in American Samoa in June 1995 and continues to reside there. John lives by himself in a house he rents in Pago Pago. He does not maintain a home outside of American Samoa. John took a 2-week vacation to New Zealand from November 11 to November 25. That was his only trip outside of American Samoa.
- 2) His wages during 1996 were \$24,000. Since these wages were from Samoan sources, they are entered on Form 4563, line 7.
- 3) He received dividends from possession corporations during 1996 as listed below. The corporations did business only in the possessions. The figures are entered on line 9 of Form 4563.

Dividends from Possession Corporations	
CNMI Corporation	\$100
Samoan Corporation	220

During 1996, he received dividends of \$12,800 from a U.S. corporation.

John adds the possession income on lines 7 and 9 and enters the total of \$24,320 on line 15. This is the income John can exclude from his gross income in 1996.

Illustrated Example of Form 8689

Bill and Jane Smith live and work in the United States. In 1996, they received \$14,400 in income from the rental of a condominium they own in the Virgin Islands. The rental income was deposited in a bank in the Virgin Islands and they received \$500 of interest on this income. They were not bona fide residents of the Virgin Islands at the end of the year.

The Smiths complete Form 1040, *U.S. Individual Income Tax Return*, reporting their income from all sources. They report their wages, interest income, and the income and expenses from their Virgin Islands rental property (Schedule E, Form 1040).

The Smiths also complete Form 8689, *Allocation of Individual Income Tax to the Virgin Islands*, to determine how much of their U.S. tax shown on line 51 of Form 1040 (with certain adjustments) is due to the Virgin Islands.

This is the amount the Smiths must pay to the Virgin Islands.

The Smiths file their Form 1040, attaching Form 8689 and all other schedules, with the Internal Revenue Service Center, Philadelphia, PA 19255.

At the same time, they send a copy of their Form 1040 with all schedules, including Form 8689, to:

Virgin Islands Bureau of Internal Revenue
9601 Estate Thomas
Charlotte Amalie
St. Thomas, U.S. Virgin Islands 00802

This copy will be processed as their original Virgin Islands return.

Form 8689. To complete their Form 8689, Bill and Jane Smith begin by entering their names, present home address, and social security numbers at the top of the form.

Part I—The Smiths enter their income from the Virgin Islands in Part I. This consists of the \$500 of interest income from a Virgin Islands bank and the net rental income from Schedule E. The interest income is entered on line 2 and the net rental income of \$6,200 (\$14,400 of rental income minus \$8,200 of rental expenses) is entered on line 11. The Smiths' total Virgin Islands income of \$6,700 is entered on line 16.

Part II—The Smiths have no adjustments to their Virgin Islands income, so they enter zero (–0–) on line 23, and \$6,700 on line 24. Their Virgin Islands adjusted gross income is \$6,700.

Part III—On line 25, the Smiths enter the amount from line 51, Form 1040 (\$5,833). The amount on Form 8689, line 25, is before any credit for taxes paid to the Virgin Islands.

The Smiths enter their worldwide adjusted gross income, \$49,737, (line 32, Form 1040) on line 28. They divide their Virgin Islands adjusted gross income, \$6,700 (from line 24), by line 28. This decimal, .135, is then multiplied by the amount on line 27 to arrive at the amount of tax due to the Virgin Islands (line 30). The Smiths include this amount in the total on Form 1040, line 58. On the dotted line next to line 58, they write "Form 8689" and show the amount. The Smiths do not complete Form 1116, *Foreign Tax Credit*.

Part IV—Part IV is used to show payments of income tax to the Virgin Islands only. The Smiths had no tax withheld by the Virgin Islands, but made estimated tax payments to the Virgin Islands of \$750, which are shown on lines 32 and 34. The income tax the Smiths owe to the Virgin Islands (\$37) is shown on line 38. They must pay their Virgin Islands tax at the same time they file the copy of their return with the Virgin Islands.

**Exclusion of Income for Bona Fide Residents
of American Samoa**

OMB No. 1545-0173

Department of the Treasury
Internal Revenue Service

▶ Attach to Form 1040. ▶ See instructions below and on back.

Attachment
Sequence No. **68**

Name(s) shown on Form 1040

John Black

Your social security number

111 00 111

Part I General Information

- 1 Date bona fide residence began ▶ **6-2-95** and ended ▶ **not ended**
- 2 Type of living quarters in American Samoa ▶ Rented room Rented house or apartment
 Quarters furnished by employer Purchased home
- 3a Did any of your family live with you in American Samoa during any part of the tax year? Yes No
b If "Yes," who and for what period? ▶
- 4a Did you maintain any home(s) outside American Samoa? Yes No
b If "Yes," show address of your home(s), whether it was rented, the name of each occupant, and his or her relationship to you. ▶
- 5 Name and address of employer (state if self-employed) ▶ **Samoa Products Co, Pago Pago, American Samoa**
- 6 Complete columns (a) through (d) below for days absent from American Samoa during the tax year.

(a) Date left	(b) Date returned	(c) Number of days absent	(d) Reason for absence
11-11-96	11-25-96	14	Vacation to New Zealand

Part II Figure Your Exclusion. Include only income that qualifies for the exclusion. See instructions.

7 Wages, salaries, tips, etc.	7	24,000
8 Taxable interest income	8	
9 Dividend income	9	320
10 Rent and royalty income	10	
11 Business income	11	
12 Farm income	12	
13 Capital gains	13	
14 Other income. List type and amount ▶	14	
15 Add lines 7 through 14. This is the amount you may exclude from your gross income this tax year. ▶	15	24,320

Instructions

Section references are to the Internal Revenue Code.

Paperwork Reduction Act Notice

We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is:

- Recordkeeping 33 min.
- Learning about the law or the form 7 min.
- Preparing the form 25 min.
- Copying, assembling, and sending the form to the IRS 17 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write or call the IRS. See the Instructions for Form 1040.

Purpose of Form

If you qualify, use Form 4563 to figure the amount of income you may exclude from your gross income.

Allocation of Individual Income Tax to the Virgin Islands

1996

▶ Attach to Form 1040.

Department of the Treasury
Internal Revenue Service

For calendar year 1995, or fiscal year ending _____, 19__

Attachment
Sequence No. 85

Your first name and initial Bill Smith		Last name	Your social security number 222 00 2222
If a joint return, spouse's first name and initial Jane Smith		Last name	Spouse's social security number 222 00 2223
Present home address (number and street) 1040 Elm St.	Apt. no.	City, town or post office, state, or territory, and ZIP code Oldtown, VA 22000	

Part I Income From the Virgin Islands

1	Wages, salaries, tips, etc.	1	
2	Taxable interest income	2	500
3	Dividend income	3	
4	Taxable refunds, credits, or offsets of local Virgin Islands taxes	4	
5	Alimony received	5	
6	Business income or (loss)	6	
7	Capital gain or (loss)	7	
8	Other gains or (losses)	8	
9	IRA distributions (taxable amount)	9	
10	Pensions and annuities (taxable amount)	10	
11	Rental real estate, royalties, partnerships, S corporations, trusts, etc.	11	6,200
12	Farm income or (loss)	12	
13	Unemployment compensation	13	
14	Social security benefits (taxable amount)	14	
15	Other income. List type and amount. ▶	15	
16	Add lines 1 through 15. This is your total income.	16	6,700

Part II Adjustments to Income From the Virgin Islands

17a	Your IRA deduction	17a	
b	Spouse's IRA deduction	17b	
18	Moving expenses	18	
19	One-half of self-employment tax	19	
20	Self-employed health insurance deduction	20	
21	Keogh retirement plan and self-employed SEP deduction	21	
22	Penalty on early withdrawal of savings	22	
23	Add lines 17a through 22. These are your total adjustments	23	-0-
24	Subtract line 23 from line 16. This is your adjusted gross income	24	6,700

Part III Allocation of Tax to the Virgin Islands

25	Enter amount from Form 1040, line 51	25	5,833
26	Enter the total of the amounts from Form 1040, lines 46, 47, and 54; any uncollected employee social security and Medicare or RRTA tax or tax on golden parachute payments included on line 51; and any amount from Form 5329, Parts II, III, or IV, included on line 48	26	
27	Subtract line 26 from line 25	27	5,833
28	Enter amount from Form 1040, line 32	28	49,737
29	Divide line 27 above by line 28. Enter the result as a decimal (carry to 3 places)	29	x .135
30	Multiply line 27 by line 29. This is your tax allocated to the Virgin Islands. Also, include this amount in the total on Form 1040, line 58. On the dotted line next to line 58, enter "Form 8689" and show the amount ▶	30	787

Part IV Payments of Income Tax to the Virgin Islands

31	Income tax withheld by the Virgin Islands	31	
32	1995 estimated tax payments and amount applied from 1995 return	32	750
33	Amount paid with Form 4868 (extension request)	33	
34	Add lines 31 through 33. These are your total payments	34	750
35	If line 34 is more than line 30, subtract line 30 from line 34. This is the amount you OVERPAID to the Virgin Islands	35	
36	Amount of line 35 you want REFUNDED TO YOU	36	
37	Amount of line 35 you want APPLIED TO YOUR 1996 ESTIMATED TAX ▶	37	
38	If line 30 is more than line 34, subtract line 34 from line 30. This is the AMOUNT YOU OWE to the Virgin Islands	38	37

Tax Publications for Individual Taxpayers

General Guides

- 1 Your Rights as a Taxpayer
- 17 Your Federal Income Tax (For Individuals)
- 225 Farmer's Tax Guide
- 334 Tax Guide for Small Business
- 509 Tax Calendars for 1997
- 553 Highlights of 1996 Tax Changes
- 595 Tax Highlights for Commercial Fishermen
- 910 Guide to Free Tax Services

Specialized Publications

- 3 Armed Forces' Tax Guide
- 378 Fuel Tax Credits and Refunds
- 483 Travel, Entertainment, Gift, and Car Expenses
- 501 Exemptions, Standard Deduction, and Filing Information
- 502 Medical and Dental Expenses
- 503 Child and Dependent Care Expenses
- 504 Divorced or Separated Individuals
- 505 Tax Withholding and Estimated Tax
- 508 Educational Expenses
- 514 Foreign Tax Credit for Individuals
- 516 U.S. Government Civilian Employees Stationed Abroad
- 517 Social Security and Other Information for Members of the Clergy and Religious Workers
- 519 U.S. Tax Guide for Aliens
- 520 Scholarships and Fellowships
- 521 Moving Expenses
- 523 Selling Your Home
- 524 Credit for the Elderly or the Disabled
- 525 Taxable and Nontaxable Income
- 526 Charitable Contributions
- 527 Residential Rental Property

- 529 Miscellaneous Deductions
- 530 Tax Information for First-Time Homeowners
- 531 Reporting Tip Income
- 533 Self-Employment Tax
- 534 Depreciating Property Placed in Service Before 1987
- 537 Installment Sales
- 541 Partnerships
- 544 Sales and Other Dispositions of Assets
- 547 Casualties, Disasters, and Thefts
- 550 Investment Income and Expenses
- 551 Basis of Assets
- 552 Recordkeeping for Individuals
- 554 Older Americans' Tax Guide
- 555 Federal Tax Information on Community Property
- 556 Examination of Returns, Appeal Rights, and Claims for Refund
- 559 Survivors, Executors, and Administrators
- 560 Retirement Plans for the Self-Employed
- 561 Determining the Value of Donated Property
- 564 Mutual Fund Distributions
- 570 Tax Guide for Individuals With Income From U.S. Possessions
- 575 Pension and Annuity Income (Including Simplified General Rule)
- 584 Nonbusiness Disaster, Casualty, and Theft Loss Workbook
- 587 Business Use of Your Home (Including Use by Day-Care Providers)
- 590 Individual Retirement Arrangements (IRAs)
- 593 Tax Highlights for U.S. Citizens and Residents Going Abroad

- 594 Understanding the Collection Process
- 596 Earned Income Credit
- 721 Tax Guide to U.S. Civil Service Retirement Benefits
- 901 U.S. Tax Treaties
- 907 Tax Highlights for Persons with Disabilities
- 908 Bankruptcy Tax Guide
- 911 Direct Sellers
- 915 Social Security and Equivalent Railroad Retirement Benefits
- 919 Is My Withholding Correct for 1997?
- 925 Passive Activity and At-Risk Rules
- 928 Household Employer's Tax Guide
- 929 Tax Rules for Children and Dependents
- 936 Home Mortgage Interest Deduction
- 946 How To Depreciate Property
- 947 Practice Before the IRS and Power of Attorney
- 950 Introduction to Estate and Gift Taxes
- 967 IRS Will Figure Your Tax
- 1542 Per Diem Rates
- 1544 Reporting Cash Payments of Over \$10,000
- 1545 How to use the Problem Resolution Program of the IRS

Spanish Language Publications

- 1SP Derechos del Contribuyente
- 579SP Cómo Preparar la Declaración de Impuesto Federal
- 594SP Comprendiendo el Proceso de Cobro
- 596SP Crédito por Ingreso del Trabajo
- 850 English-Spanish Glossary of Words and Phrases Used in Publications Issued by the Internal Revenue Service

Commonly Used Tax Forms

- 1040 U.S. Individual Income Tax Return
 - Sch A Itemized Deductions
 - Sch B Interest and Dividend Income
 - Sch C Profit or Loss From Business
 - Sch C-EZ Net Profit From Business
 - Sch D Capital Gains and Losses
 - Sch E Supplemental Income and Loss
 - Sch EIC Earned Income Credit
 - Sch F Profit or Loss From Farming
 - Sch H Household Employment Taxes
 - Sch R Credit for the Elderly or the Disabled
 - Sch SE Self-Employment Tax
- 1040EZ Income Tax Return for Single and Joint Filers With No Dependents
- 1040A U.S. Individual Income Tax Return
 - Sch 1 Interest and Dividend Income for Form 1040A Filers

- Sch 2 Child and Dependent Care Expenses for Form 1040A Filers
- Sch 3 Credit for the Elderly or the Disabled for Form 1040A Filers
- 1040-ES Estimated Tax for Individuals
- 1040X Amended U.S. Individual Income Tax Return
- 2106 Employee Business Expenses
- 2106-EZ Unreimbursed Employee Business Expenses
- 2119 Sale of Your Home
- 2210 Underpayment of Estimated Tax by Individuals, Estates, and Trusts
- 2441 Child and Dependent Care Expenses
- 2848 Power of Attorney and Declaration of Representative
- 3903 Moving Expenses
- 4562 Depreciation and Amortization

- 4868 Application for Automatic Extension of Time To File U.S. Individual Income Tax Return
- 4952 Investment Interest Expense Deduction
- 5329 Additional Taxes Attributable to Qualified Retirement Plans (Including IRAs), Annuities, and Modified Endowment Contracts
- 6251 Alternative Minimum Tax-Individuals
- 6283 Noncash Charitable Contributions
- 8582 Passive Activity Loss Limitations
- 8606 Nondeductible IRAs (Contributions, Distributions, and Basis)
- 8822 Change of Address
- 8929 Expenses for Business Use of Your Home

How To Get Forms, Publications, and Other Information



You can get information from the IRS in several ways. Choose the method from the table below that is best for you.

Method	Type of Information	How To Get the Information								
• By phone	• Forms and publications	▶ Call 1-800-TAX-FORM (1-800-829-3676) during regular business hours. If you have access to TTY/TDD equipment, you can call 1-800-829-4059 .								
	• Tele-Tax topics	▶ See your income tax package for the phone number and list of Tele-Tax topics.								
	• Personal assistance	▶ Call 1-800-829-1040 during regular business hours. If you have access to TTY/TDD equipment, you can call 1-800-829-4059 .								
• By mail	• Forms and publications	▶ Write to the IRS Forms Distribution Center listed for your state. Print or type your name and address clearly and indicate the number of the form or publication, i.e., Form 1040 or Publication 463. <table border="0"> <tr> <td><i>Address</i></td> <td><i>States (abbreviated)</i></td> </tr> <tr> <td>Western Area Distribution Center Rancho Cordova, CA 95743-0001</td> <td>AK, AZ, CA, CO, HI, ID, MT, NV, NM, OR, UT, WA, WY, Guam, Northern Marianas, American Samoa</td> </tr> <tr> <td>Central Area Distribution Center P.O. Box 8903 Bloomington, IL 61702-8903</td> <td>AL, AR, IL, IN, IA, KS, KY, LA, MI, MN, MS, MO, NE, ND, OH, OK, SD, TN, TX, WI</td> </tr> <tr> <td>Eastern Area Distribution Center P.O. Box 85074 Richmond, VA 23261-5074</td> <td>CT, DE, DC, FL, GA, ME, MD, MA, NH, NJ, NY, NC, PA, RI, SC, VT, VA, WV</td> </tr> </table> <p>If you live in any other location, see your Income tax package for the address.</p>	<i>Address</i>	<i>States (abbreviated)</i>	Western Area Distribution Center Rancho Cordova, CA 95743-0001	AK, AZ, CA, CO, HI, ID, MT, NV, NM, OR, UT, WA, WY, Guam, Northern Marianas, American Samoa	Central Area Distribution Center P.O. Box 8903 Bloomington, IL 61702-8903	AL, AR, IL, IN, IA, KS, KY, LA, MI, MN, MS, MO, NE, ND, OH, OK, SD, TN, TX, WI	Eastern Area Distribution Center P.O. Box 85074 Richmond, VA 23261-5074	CT, DE, DC, FL, GA, ME, MD, MA, NH, NJ, NY, NC, PA, RI, SC, VT, VA, WV
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Eastern Area Distribution Center P.O. Box 85074 Richmond, VA 23261-5074	CT, DE, DC, FL, GA, ME, MD, MA, NH, NJ, NY, NC, PA, RI, SC, VT, VA, WV									
• Forms and publications	▶ The post office is a good source of the most common forms and schedules. The library stocks a wider variety of forms and some publications that you may photocopy. It may also have a CD-ROM from which you can view or print items. The CD contains forms from 1991 to the present and publications from 1994 to the present.									
• With a computer and modem	• Forms and publications	▶ Use the Internet— World Wide Web — http://www.irs.ustreas.gov Telnet — irs.irs.ustreas.gov FTP — ftp.irs.ustreas.gov <i>TIP:</i> If you subscribe to an on-line service, ask your provider how to best access IRS information. ▶ Access the Internal Revenue Information Services bulletin board at 703-321-8020 (not toll-free). <i>TIP:</i> If you're a new user, you may want to read the on-line help first.								
	• Educational materials									
• By fax	• IRS press releases and fact sheets									
	• Tele-Tax topics									
• By fax	• Forms and other information	▶ Dial 703-467-4160 (not toll-free) from your fax machine to reach IRS Tax Fax. You can request up to 3 items during each call. This fax program provides 100 of the most popular forms and instructions (not publications), as well as other information, 24 hours a day, seven days a week.								
	• Tele-Tax topics	▶ See your income tax package for a list of Tele-Tax topics.								