

# HR & Tax Alert



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## United States: Guidance Clarifies U.S. Limitations Period on Assessment for USVI Taxpayers

April 2007

The Internal Revenue Service (IRS) has announced that for tax years ending on or after December 31, 2006, the U.S. federal statute of limitations for all U.S. citizens and residents claiming to be bona fide residents of the U.S. Virgin Islands (USVI) will generally commence upon the filing of an income tax return with the USVI (Notice 2007-31).

The notice amends and supplements Notice 2007-19, issued February 21, 2007, which provided interim rules under Sections 932(c) and 7654(e) regarding the statute of limitations on assessment for taxpayers claiming to be bona fide residents of the USVI. Since issuance of the notice, the USVI Bureau of Internal Revenue (BIR) and the IRS have entered into a new working arrangement (Working Arrangement) concerning the routine (automatic) exchange of information under the Tax Implementation Agreement between the United States and the USVI dated February 24, 1987.

### Working Arrangement and Interim Rules

The Working Arrangement applies to tax years ending on or after December 31, 2006. It establishes a new routine exchange of information program between the IRS and the USVI BIR concerning income tax information of certain taxpayers who file an income tax return with the USVI under Section 932(c)(2).

Under interim rules, an individual income tax return filed under Section 932(c)(2) with the USVI by a U.S. citizen or resident alien (USVI 1040) who takes the position that he or she is a bona fide resident of the USVI for the entire tax year (or an individual who files a joint return for the tax year with such an individual) will be deemed to be a U.S. income tax return of that individual for purposes of the three-year period of limitations under Section 6501(a). The notice provides that in the event the Working Arrangement is terminated and there is no successor agreement, the interim rules in Notice 2007-19 will apply.

### Effective Date

Notice 2007-31 applies to tax years ending on or after December 31, 2006. For tax years ending before December 31, 2006, a taxpayer may choose to apply the interim rules provided in Notice 2007-19.

Under those rules, a “non-covered person’s” (a bona fide resident of the USVI with gross income of \$75,000 or more) filed U.S. Form 1040 will be treated as an income tax return described in Section 6501(a). The return filed by the non-covered person reports no gross income and no taxable income in the U.S. In addition, the return must include a statement of facts substantiating the USVI bona fide residence claim and be signed under penalties of perjury.

A “covered person” (a U.S. citizen or resident alien who takes the position that he or she is a bona fide resident of the USVI, files USVI Form 1040 with the USVI, and has less than \$75,000 in gross income for the tax year) that chooses to apply the interim rules of Notice 2007-19 to a tax year ending before December 31, 2006, must be able to provide documentation upon examination that establishes to the Commissioner’s satisfaction, that the taxpayer is a covered person.

### **Next Steps**

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The Working Arrangement allows for a simpler process for establishing the statute of limitations on assessment of U.S. income tax than the interim rules of Notice 2007-19 set forth, particularly for individuals with gross income of \$75,000 or more (non-covered persons). For tax years prior to 2006, non-covered persons should consider whether it is appropriate to file prior year U.S. income tax returns in accordance with Notice 2007-19.

For further information, please contact your local Ernst & Young Human Capital professional.

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