

Foreign Tax Credit Computation Worksheet

Form 1116		Foreign Tax Credit (Individual, Estate, or Trust)		OMB No. 1545-0121
Department of the Treasury Internal Revenue Service (IRS)		▶ Attach to Form 1040, 1040NR, 1041, or 990-T. ▶ Go to www.irs.gov/Form1116 for instructions and the latest information.		2018 Attachment Sequence No. 19
Name Amy		Identifying number as shown on page 1 of your tax return 000-00-0000		
Use a separate Form 1116 for each category of income listed below. See Categories of Income in the instructions. Check only one box on each Form 1116. Report all amounts in U.S. dollars except where specified in Part II below.				
<input type="checkbox"/> Section 951A income		<input type="checkbox"/> Passive category income		<input type="checkbox"/> Section 901(g) income
<input type="checkbox"/> Foreign branch income		<input checked="" type="checkbox"/> General category income		<input type="checkbox"/> Lump-sum distributions
<input type="checkbox"/> Foreign branch income		<input type="checkbox"/> Certain income re-sourced by treaty		
h Resident of (name of country) ▶ Canada				
Note: If you paid taxes to only one foreign country or U.S. possession, use column A in Part I and line A in Part II. If you paid taxes to more than one foreign country or U.S. possession, use a separate column and line for each country or possession.				
Part I Taxable Income or Loss From Sources Outside the United States (for category checked above)				
i Enter the name of the foreign country or U.S. possession ▶ Canada		Foreign Country or U.S. Possession		Total (Add cols. A, B, and C.)
		A	B	C
1a Gross income from sources within country shown above and of the type checked above (see instructions): GENERAL INCOME (WAGES)				
		140,000		140,000
b Check if line 1a is compensation for personal services as an employee, your total compensation from all sources is \$250,000 or more, and you used an alternative basis to determine its source (see instructions) ▶ <input type="checkbox"/>				
Deductions and losses (Caution: See instructions.)				
2 Expenses definitely related to the income on line 1a (attach statement)				
3 Pro rata share of other deductions not definitely related :				
a Certain itemized deductions or standard deduction (see instructions)		12,000		
b Other deductions (attach statement)				
c Add lines 3a and 3b		12,000		
d Gross foreign source income (see instructions)		140,000		
e Gross income from all sources (see instructions)		144,000		
f Divide line 3d by line 3e (see instructions)		0.97222		
g Multiply line 3c by line 3f		11,666		
4 Pro rata share of interest expense (see instructions):				
a Home mortgage interest (use the Worksheet for Home Mortgage Interest in the instructions)				
b Other interest expense				
5 Losses from foreign sources				
6 Add lines 2, 3g, 4a, 4b, and 5		11,666		11,666
7 Subtract line 6 from line 1a. Enter the result here and on line 15, page 2				128,334

Foreign tax credit computation worksheet is an essential tool for U.S. taxpayers who have paid foreign taxes and wish to claim a credit against their U.S. tax liability. The foreign tax credit is designed to alleviate the double taxation burden on income earned abroad. Understanding how to effectively use the foreign tax credit computation worksheet can lead to significant savings for individuals and businesses operating internationally. This article provides a comprehensive guide to the foreign tax credit computation worksheet, including its purpose, the steps involved in completing it, and common considerations for taxpayers.

What is the Foreign Tax Credit?

The foreign tax credit allows U.S. taxpayers to reduce their U.S. tax liability by the amount of foreign taxes they have paid or accrued on foreign income. This credit is particularly valuable for individuals and corporations engaged in business or investment activities outside the United States.

The purpose of the foreign tax credit is to prevent double taxation, which occurs when the same income is taxed by both the U.S. and a foreign country. By claiming this credit, taxpayers can effectively offset their U.S. tax liability with the taxes they have already paid to foreign governments.

Who Can Benefit from the Foreign Tax Credit?

The foreign tax credit is beneficial for various groups, including:

- U.S. citizens living abroad
- U.S. residents earning foreign income
- Corporations with foreign subsidiaries or investments
- Partnerships and S corporations with foreign income

Each of these groups may have unique circumstances that impact their eligibility and the amount of credit they can claim.

Understanding the Foreign Tax Credit Computation Worksheet

The foreign tax credit computation worksheet is a detailed form that helps taxpayers calculate the credit they are entitled to based on their foreign income and taxes paid. The worksheet is typically included with IRS Form 1116, which is used to claim the foreign tax credit.

Key Sections of the Foreign Tax Credit Computation Worksheet

The worksheet consists of several key sections that guide taxpayers through the calculation process:

1. Part I: Foreign Tax Paid or Accrued
 - This section requires taxpayers to list the foreign taxes paid or accrued during the tax year. It includes information about the foreign income sources and the corresponding tax amounts.
2. Part II: Foreign Source Income
 - Taxpayers must report their foreign source income in this section. This includes wages, interest, dividends, and any other income earned from foreign sources.
3. Part III: Limit on Foreign Tax Credit
 - This part helps determine the amount of foreign tax credit that can be claimed based on the taxpayer's total foreign income and U.S. tax liability.
4. Part IV: Carryover of Unused Foreign Taxes
 - If the foreign tax credit exceeds the limit, this section allows taxpayers to calculate any unused foreign taxes that can be carried over to future tax years.

Steps to Complete the Foreign Tax Credit Computation Worksheet

Completing the foreign tax credit computation worksheet requires careful attention to detail. Below are the steps to follow:

1. **Gather Documentation:** Collect all relevant tax documents, including foreign tax returns, income statements, and proof of taxes paid.
2. **Determine Foreign Taxes Paid:** Identify the amount of foreign taxes you have paid or accrued during the tax year. This may include withholding taxes and income taxes imposed by the foreign country.
3. **Report Foreign Source Income:** List all foreign source income on the worksheet. Ensure that you report income in the correct categories (e.g., wages, dividends, etc.). This income should be converted to U.S. dollars using the appropriate exchange rates.
4. **Calculate the Foreign Tax Credit Limit:** Use the formula provided in the worksheet to determine the foreign tax credit limit. This is based on the ratio of foreign source income to total income.
5. **Complete the Worksheet:** Fill out each section of the worksheet accurately. Check for any inconsistencies or errors in your calculations.
6. **File with Your Tax Return:** Attach the completed worksheet to your tax return (Form 1040 or corporate return) to claim the foreign tax credit.

Common Considerations When Using the Foreign Tax Credit Computation Worksheet

While the foreign tax credit computation worksheet is a valuable tool, there are several important considerations to keep in mind:

1. Eligibility Criteria

Not all foreign taxes qualify for the credit. The IRS has specific guidelines on what constitutes an eligible foreign tax. Generally, the tax must be a legal and actual foreign tax imposed on income. Taxes that are considered to be more like penalties or are refundable do not qualify.

2. High-Income Taxpayers

For high-income taxpayers, the foreign tax credit may be subject to limitations. It's crucial to consult IRS guidelines to determine how these limitations may apply to your specific situation.

3. Separate Limitation Requirement

Taxpayers must separate their foreign source income into categories (e.g., passive income, general income). Each category has its own limit for the foreign tax credit, which can complicate the computation process.

4. Currency Conversion

Foreign income and taxes must be reported in U.S. dollars. Taxpayers should use the appropriate exchange rates for the specific dates of their foreign income and tax payments to ensure accurate reporting.

5. Record-Keeping

Maintaining accurate and organized records of foreign income and taxes paid is essential. This documentation is crucial in case of an audit by the IRS or if any questions arise about the credit claimed.

Conclusion

The foreign tax credit computation worksheet is an invaluable resource for U.S. taxpayers who earn income abroad and wish to mitigate the impact of double taxation. By understanding the worksheet's sections, following the completion steps carefully, and being aware of common considerations, taxpayers can maximize their foreign tax credit and ensure compliance with IRS regulations.

As international business and cross-border investments continue to grow, the importance of effectively managing foreign tax credits will only increase. Taxpayers should consider consulting with tax professionals to navigate complex foreign tax issues and optimize their tax situations.

Frequently Asked Questions

What is a foreign tax credit computation worksheet?

A foreign tax credit computation worksheet is a tool used by taxpayers to calculate the foreign tax credit they are eligible to claim on their U.S. tax return, allowing them to offset taxes paid to foreign governments against U.S. tax liability.

Who needs to use the foreign tax credit computation worksheet?

Taxpayers who have paid foreign taxes on income earned outside the U.S. and wish to claim a foreign tax credit to reduce their U.S. tax liability should use the worksheet.

What information is required to complete the foreign tax credit computation worksheet?

To complete the worksheet, taxpayers need information such as the amount of foreign taxes paid, type of income earned, and any relevant deductions or credits that may affect the computation.

Can the foreign tax credit be carried over to future years?

Yes, if the foreign tax credit exceeds the limit for the current tax year, it can be carried back one year or carried forward up to 10 years to offset future U.S. tax liabilities.

What is the maximum foreign tax credit a taxpayer can claim?

The maximum foreign tax credit a taxpayer can claim is generally limited to the amount of U.S. tax attributable to foreign-sourced income, calculated using the foreign tax credit limitation rules.

Are there any common mistakes to avoid when filling out the foreign tax credit computation worksheet?

Common mistakes include miscalculating foreign taxes paid, overlooking the foreign tax credit limitation, and failing to include all relevant foreign income types, which can lead to an inaccurate credit claim.

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