Howkins v. Commissioner, 40 T. C. 965 (1963)

The source of alimony payments for tax withholding purposes is determined by the residence of the payer, not the location of the funds used to make the payment.

Summary

In Howkins v. Commissioner, the court addressed whether alimony payments made by a U. S. resident to a nonresident alien ex-wife from a foreign bank account constituted income from U. S. sources, subject to withholding tax. The court ruled that the source of such payments is the residence of the payer, not the location of the funds. The petitioner, who made payments from an account in England, was liable for withholding U. S. tax because he was a U. S. resident. The decision emphasized that the payer's residence, not the funds' origin, determines the income's source for tax purposes.

Facts

Petitioner, a U. S. resident, agreed in 1949 to pay his then-wife, a resident of England, $100 monthly alimony. After their 1950 divorce, he made these payments from an account in England. Petitioner claimed alimony deductions in his U. S. tax returns but did not withhold U. S. tax on these payments to his nonresident alien ex-wife. The Commissioner assessed deficiencies for failure to withhold tax at source for the years 1950-1961.

Procedural History

The Commissioner determined deficiencies against the petitioner for failure to withhold tax on alimony payments to his nonresident alien ex-wife. The case was brought before the Tax Court to decide whether these payments constituted income from sources within the United States.

Issue(s)

1. Whether alimony payments made by a U. S. resident to a nonresident alien from a foreign bank account constitute gross income from sources within the United States, subject to withholding tax.

Holding

1. Yes, because the source of the alimony payments is determined by the residence of the payer, not the location of the funds used to make the payment. The petitioner, as a U. S. resident, was obligated to withhold U. S. tax on these payments.

Court's Reasoning

The court reasoned that the source of income for tax purposes is where the income is “produced,” not the origin of the funds used for payment. The court cited the statutory source-of-income rules for interest payments, where the residence of the obligor determines the source, as a persuasive analogy. The court emphasized that the petitioner’s obligation to pay alimony stemmed from a U. S. divorce decree and his U. S. residence, thus classifying the payments as income from U. S. sources. The court rejected the petitioner’s argument that the payments were from foreign sources because they were made from a foreign account, stating, “The real and immediate ‘source’ of the alimony was petitioner himself, a resident of the United States. ” The court also dismissed the petitioner’s claim about the funds being “blocked” due to insufficient evidence that he could not have used other U. S. funds or obtained permission to use the withheld amount for tax payment.

Practical Implications

This ruling clarifies that for tax withholding purposes, the residence of the payer, not the location of the payment funds, determines the source of alimony payments. Legal practitioners must advise clients that alimony paid to nonresident aliens by U. S. residents is subject to U. S. withholding tax, regardless of where the funds are drawn from. This decision impacts how alimony agreements are structured and the tax planning strategies for U. S. residents paying alimony to nonresident aliens. It also affects how similar cases involving other types of periodic payments are analyzed, reinforcing the principle that the source of income is tied to the payer’s residence. Subsequent cases have applied this principle, notably in situations involving other forms of income paid to nonresident aliens.