Foreign Investment in Real Property Tax Act

<u>FIRPTA Rules</u>

Purchasing property in the United States by a foreign buyer or seller (est. 1980).
FIRPTA, the Foreign Investment in Real Property Transfer Act, is part of the U.S. tax code. It requires **<u>buyers</u>** of real estate to withhold up to 15% of the sales price when a **<u>seller is a foreign person (not a U.S. citizen or U.S. resident)</u>** under Section 1445 of the IRS code.

The buyer is the person ultimately responsible to have this tax withheld at the closing and remit to the IRS within 20 days after the closing. If the IRS is unable to collect the taxes owed from the sale, then the buyer is responsible for the tax, plus interest.

Therefore, if you are buying or selling commercial or residential real estate, it's important to understand the requirements of FIRPTA.

If the seller is a U.S. citizen, U.S. entity or Resident Alien, then the seller should complete a certificate of Non-Foreign Status.

<u>If you represent the seller:</u>

If the Seller – US Person – No issue
If Seller – Foreign Person – Subject to FIRPTA

<u>If you represent the buyer:</u>

If Seller is a foreign person – Buyer is subject to FIRPTA
If Buyer is a foreign person – Subject to US tax rules

<u>Which percentage to withhold, 0%, 10% or 15%?</u>

If the sales price is $300,000 or less and the buyer intends to use the property as their residence, then 0% withholding* is required, providing the buyer signs a declaration of intent to reside.

However, if the buyer will not use this property as their property as their primary residence, such as a rental property, then 15% must be withheld.

* Note: The buyer (or member of the buyer's family) must reside in the property for at least 50% of the number days the property is used by any person during the 24 months following the date of the transfer.

If the sales price is $300,001 - $1,000,000 and the buyer intends to use the property as their residence, then 10% withholding* is required, providing the buyer signs a declaration of intent to reside.

However, if the buyer will not use this property as their property as their primary residence, then 15% must be withheld at the closing.

If the sales price is $1,000,000 or more, then 15% withholdings is required, regardless if this will be the buyer's primary residence or not.

<u>Form 8288 – U.S. Withholding Tax Return for Dispositions by Foreign Persons of U.S. real Property interests</u>

The form 8288 needs to be provided to the IRS within 20 days after the transfer of property to provide the IRS information such as:

- The name of the buyer, their address and tax id number.
- The description of the property – type of property (condo, co-op, etc.) and property address.
- Date of the transfer and sales price.
- Withholding percentage used and amount withheld.

Form 8288-A (Statement of withholdings) – this form goes with form 8288 to provide the withholding agent (usually buyers attorney) and person subject to the withholding names (seller), address, tax id numbers, amount realized, and federal taxes withheld.

Note: There also maybe state withholding forms requirements too.

<u>Form 8288-B – U.S. Application Withholding Certificate for Dispositions by Foreign Persons of U.S. real Property interests</u>

The form 8288-B is used to apply for a withholding certificate to reduce or eliminate withholding on dispositions by foreign persons of U.S. real property interests.

This form includes, not limited to, the following information:

- The name of the transferor (seller), address and tax id number.
- The name of the transferee (buyer), address and tax id number.
- The name of the withholding agent, address and tax id number. Often the buyer's attorney.
- Description of the property such as address, type of property, date of sale, sales price and adjusted basis.

The purpose of this form is to inform the IRS of the projected profit and taxes due resulting from the sale after deducting the original cost, closing fees, renovations, carried forward losses, etc. This form needs to be filled out completely along with supporting documents on how the profit or loss and tax amount due were determined.

This will lower the withholding percentage to avoid paying in a high amount of taxes, then waiting for the income tax returns (1040 or 1040NR) to be filed, the following year, which can take months.

The form should be submitted to the IRS as early as possible, as it takes time for the IRS to provide their approval, usually within 120 days after the form is submitted. 20 days after the closing, the taxes withheld need to be forwarded to the IRS. If the approval is not received in a timely period, the buyer's attorney may hold the withholding taxes in an escrow account until IRS provides their decision.