

FIRPTA Changes Primer

*What They Mean for Buyers and Sellers of
Real Property and for the
Commercial Real Estate Industry*

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What is the Foreign Investment in Real Property Tax Act?



Why Was FIRPTA Enacted?

In late 1970s,

- Increased foreign investment in U.S. real property greatly alarmed some Americans
- Became national topic of discussion when 60 Minutes aired story about it
- Avalanche of letters to Congress demanding something be done



1979 Treasury Study



Basics of How FIRPTA Works

- Makes disposition of U.S. real property interest by foreign person subject to withholding
 - Disposition is sale, exchange, gift, etc.
- Buyer required to withhold a portion of amount realized (generally the selling price)



Policy & Political Factors of FIRPTA

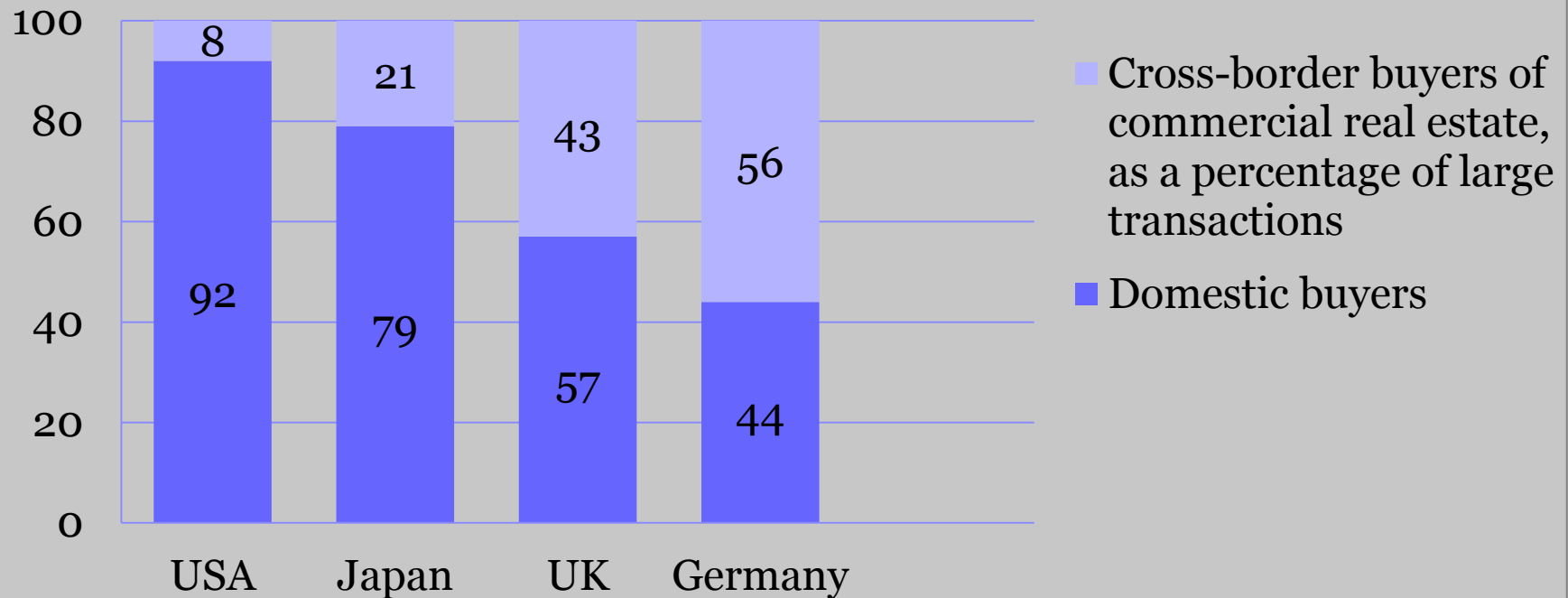
- Before FIRPTA, many foreign owners of U.S. RE not subject to tax on gains when sold
- FIRPTA was enacted to establish equity of tax treatment between foreign and domestic RE owners
- However, it has long been U.S. policy to welcome foreign investment of stocks, bonds, Treasury securities (and before FIRPTA, real estate) by not taxing capital gains



Policy Results of FIRPTA



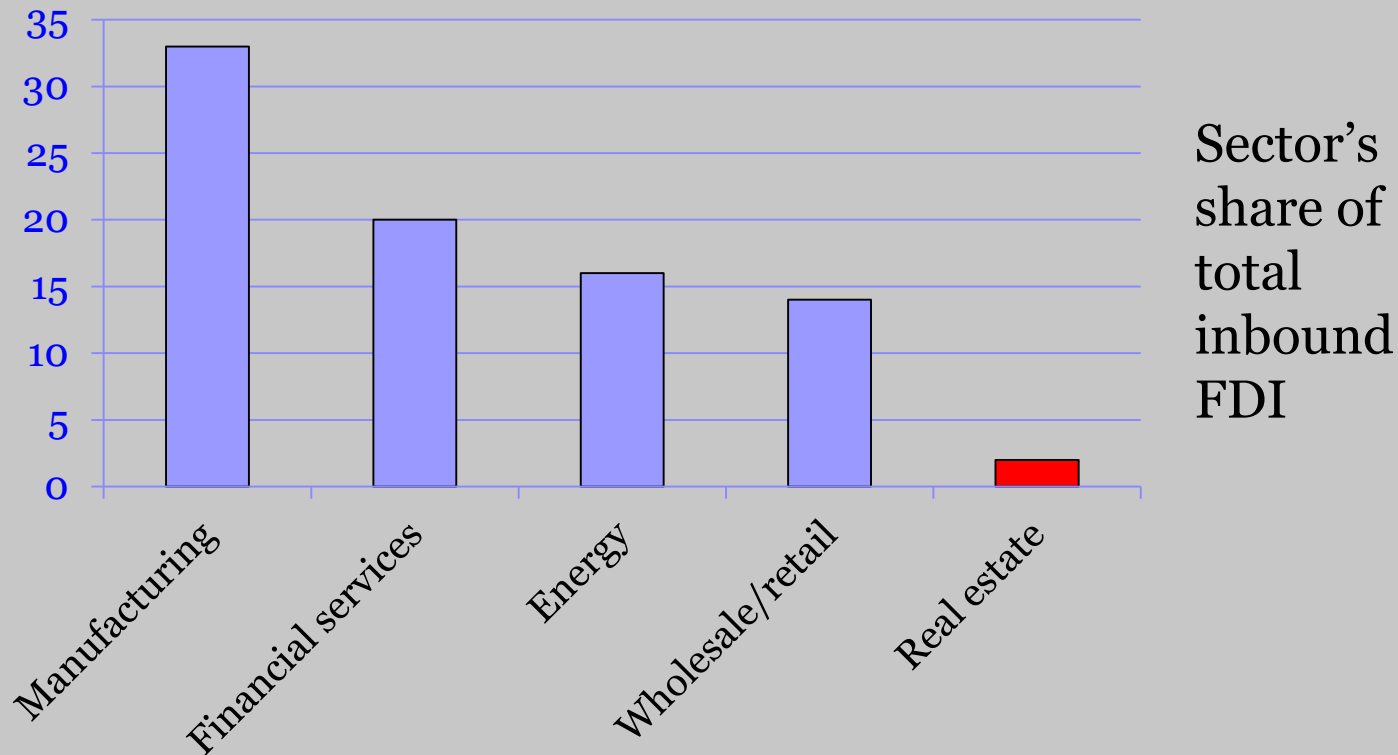
United States Behind in the Race for Global Equity Investment in Real Estate



Policy Results of FIRPTA



Real Estate Trails other U.S. Industries in Foreign Direct Investment



Source: Bureau of Economic Analysis

Coalition to Ease FIRPTA Rules



PATH Act of 2015



- Protecting American Taxpayers from Tax Hikes Act
- Signed into law 12/18/15
- Extended retroactively over 50 expired tax provisions
- Included FIRPTA provisions

FIRPTA Policy Changes to Increase Foreign Investment in U.S. Commercial RE

- Increase max holdings of foreign investor in U.S. REIT from 5% to 10% (without triggering FIRPTA)
- Allow foreign pension funds to invest in U.S. real estate without triggering FIRPTA



Now For The Details

Presumes All Sellers Are Foreign Sellers

Corporation

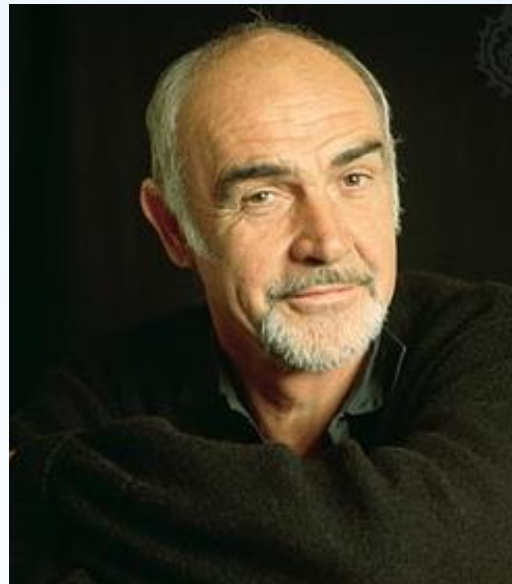


Estate

LLC

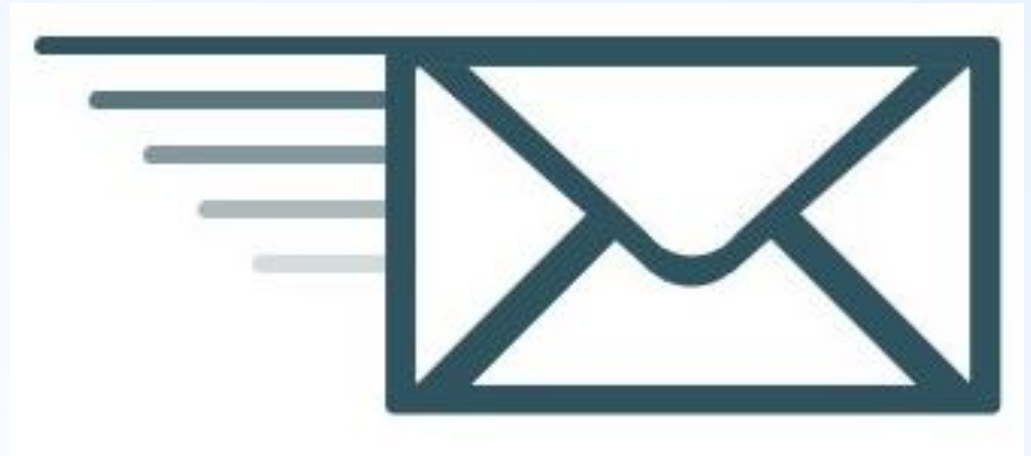


Land Trust



Partnership

Creates Duty Of Buyer To Withhold And Remit Funds To IRS



Buyer Is The Withholding Agent And Settlement Agent Usually Completes Required Tasks



Applies To All U.S. Real Estate, Some Personal Property, Includes Rents




Current Withholding Rate Is 15%



Withhold 15% OF What?

- Amount Realized
 - Contract
- Plus personal property associated with the use of the real property
- Also includes interest in mines, wells, standing timber, etc.
 - Now for more details



CALIFORNIA ASSOCIATION OF REALTORS®
CALIFORNIA RESIDENTIAL PURCHASE AGREEMENT AND JOINT ESCROW INSTRUCTIONS
 For Use With Single Family Residential Property — Attached or Detached (C.A.R. Form RPA-CA, Revised 4/10)

Date: January 1, 2013

1. OFFER:
 A. THIS IS AN OFFER FROM Buyer 1, Buyer 2 ("Buyer").
 B. THE REAL PROPERTY TO BE ACQUIRED is described as Street Address, City, CA Zip Code, situated in County of, Assessor's Parcel No. APN Number, ("Property").
 C. THE PURCHASE PRICE offered is One Million (\$ 1,000,000.00) (State) for 30 Days After Acceptance.
 D. CLOSE OF ESCROW shall occur on State (State) for 30 Days After Acceptance.

2. AGENCY:
 A. DISCLOSURE: Buyer and Seller each acknowledge prior receipt of a "Disclosure Regarding Real Estate Agency Relationships" (C.A.R. Form AD).
 B. POTENTIALLY COMPETING BUYERS AND SELLERS: Buyer and Seller each acknowledge receipt of a disclosure of the possibility of multiple representation by the Broker representing that principal. This disclosure may be part of a listing agreement, buyer representation agreement or separate document (C.A.R. Form DA). Buyer understands that Broker representing Buyer may also represent other potential buyers, who may consider, make offers on or ultimately acquire the Property. Seller understands that Broker representing Seller may also represent other sellers with competing properties of interest to this Buyer.
 C. CONFIRMATION: The following agency relationships are hereby confirmed for this transaction:
 Listing Agent: Reward Realty (Print Firm Name) is the agent of (check one): ☐ the Seller exclusively; or ☐ both the Buyer and Seller.
 Selling Agent: Reward Realty (Print Firm Name) is the agent of (check one): ☐ the Buyer exclusively; or ☐ both the Buyer and Seller. Real Estate Brokers are not parties to the Agreement between Buyer and Seller.

3. FINANCE TERMS: Buyer represents that funds will be good when deposited with Escrow Holder.
 A. INITIAL DEPOSIT: Deposit shall be in the amount of \$ 30,000.00.
 (1) Buyer shall deliver deposit directly to Escrow Holder by personal check, ☐ electronic funds transfer, ☐ Other _____.
 OR (2) (checked) ☒ Buyer has given the deposit by personal check (or ☐ Other _____) to the agent submitting the offer for ☐ _____. The deposit shall be held uncashed until Acceptance and then deposited with Escrow Holder (or ☐ into Broker's trust account) within 3 business days after Acceptance (or ☐ Other _____).
 B. INCREASED DEPOSIT: Buyer shall deposit with Escrow Holder an increased deposit in the amount of \$ _____ within _____ Days After Acceptance, or ☐ _____. If a liquidated damages clause is incorporated into this Agreement, Buyer and Seller shall sign a separate liquidated damages clause (C.A.R. Form RD) for any increased deposit at the time it is deposited.
 C. LOANS:
 (1) FIRST LOAN: in the amount of \$ 800,000.00.
 This loan will be conventional financing or, if checked, ☐ FHA ☐ VA ☐ Seller (C.A.R. Form SFA).
☐ assumed financing (C.A.R. Form PAI). ☐ Other _____. This loan shall be at a fixed rate not to exceed _____ % or ☐ an adjustable rate loan with initial rate not to exceed _____ %.
 Regardless of the type of loan, Buyer shall pay points not to exceed _____ % of the loan amount.
 (2) SECOND LOAN: in the amount of \$ _____.
 This loan will be conventional financing or, if checked, ☐ Seller (C.A.R. Form SFA). ☐ assumed financing (C.A.R. Form PAI). ☐ Other _____. This loan shall be at a fixed rate not to exceed _____ % or ☐ an adjustable rate loan with initial rate not to exceed _____ %.
 Regardless of the type of loan, Buyer shall pay points not to exceed _____ % of the loan amount.
 (3) FHA/VA: For any FHA or VA loan specified above, Buyer has 17 (or _____) Days After Acceptance to Deliver to Seller written notice (C.A.R. Form FVA) of any lender-required repairs or costs that Buyer requests Seller to pay for or repair. Seller has no obligation to pay for repairs or satisfy lender requirements unless otherwise agreed in writing.
 D. ADDITIONAL FINANCING TERMS: _____
 E. BALANCE OF PURCHASE PRICE OR DOWN PAYMENT: in the amount of \$ 170,000.00.
 To be deposited with Escrow Holder within sufficient time to close escrow.
 F. PURCHASE PRICE (TOTAL): \$ 1,000,000.00

Buyer's Initials (_____) (_____) Seller's Initials (_____) (_____)

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RPA-CA REVISED 4/10 (PAGE 1 OF 8)

CALIFORNIA RESIDENTIAL PURCHASE AGREEMENT (RPA-CA PAGE 1 OF 8)

Agent: Caroline Dukelow Phone: (855) 449-0945 Fax: _____ Prepared using zipform software
 Broker: Keller Williams 555 Hamilton Ave., Suite 100 Palo Alto, CA 94301

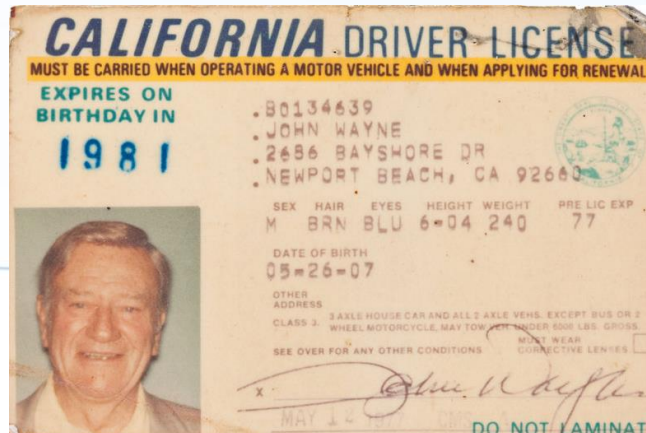
How Do I Know If My Seller Is Foreign?

- Ask
- Foreign
 - Nonresident alien individual, or
 - Foreign corporation, etc.
- Not Foreign
 - U.S. citizen
 - Resident alien (legal permanent resident)
 - Person who can meet substantial presence test
 - Unsure, check with an attorney



How Do I Know If My Seller Is Foreign?

- Non-foreign persons will
 - Produce picture ID
 - Driver's license or
 - Passport
 - Sign an affidavit at closing with their social security number



Find Out Early If Seller Is Foreign



- Listing Agent – always ask
 - In negotiations for listing
 - As setting up the property
- Cooperating Agent – always ask
 - Inquire when contract is complete

Seller Is Foreign – What Next?

- As soon as possible notify
 - Buyer's real estate agent
 - Settlement agent



Find Out Early If Seller Is Foreign

- Settlement agent will help buyer with requirements
- May need help from CPA or attorney



Seller Is Foreign – What Next?

- If seller does not already have an ITIN, they should apply
 - ITIN – Individual Tax Identification Number
 - Can take 4 to 6 weeks to obtain
- All foreign buyers are required to obtain an ITIN since 2003



Department of the Treasury
Internal Revenue Service

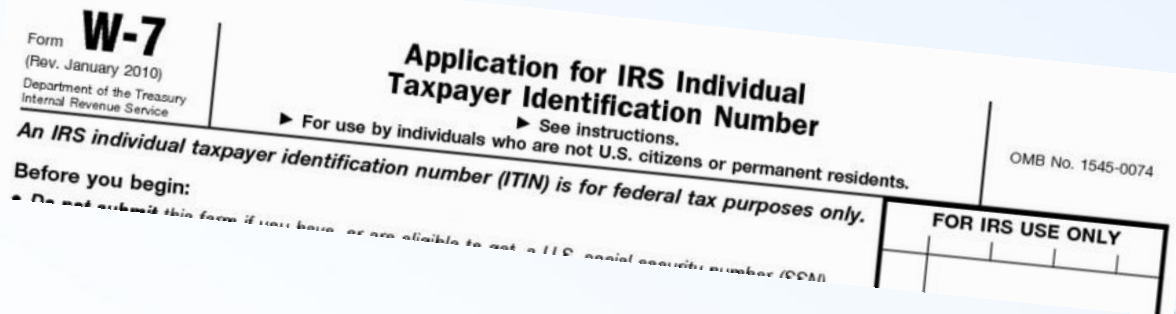
Individual Taxpayer Identification Number

999 - 99 - 9999

This number has been established for:
JOSE GONZALEZ

To be used for Tax purposes only

SAMPLE



Form **W-7**
(Rev. January 2010)
Department of the Treasury
Internal Revenue Service

Application for IRS Individual Taxpayer Identification Number

► For use by individuals who are not U.S. citizens or permanent residents. ► See instructions.

An IRS individual taxpayer identification number (ITIN) is for federal tax purposes only.

Before you begin:
• Do not submit this form if you have, or are eligible to get, a U.S. social security number (SSN).

OMB No. 1545-0074

FOR IRS USE ONLY

Seller Is Foreign – What Next?

- Closing agent or seller's agent should prepare seller for the required 15% withholding
 - Most foreign sellers are aware of the required withholding



Buyer's Duties



- Buyer will need Seller's ITIN for forms
 - Closing will **NOT** be delayed if no ITIN

Buyer's Duties

- Fill in:
 - Form 8288
 - Form 8288-A (one for each foreign seller)
- No ITIN use “applied for” in the specified blank

Form 8288 (Rev. February 2016) Department of the Treasury Internal Revenue Service	U.S. Withholding Tax Return for Dispositions by Foreign Persons of U.S. Real Property Interests ▶ Information about Form 8288 and its separate instructions is at www.irs.gov/form8288 .	OMB No. 1545-0902
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Withholding agent's name, street address, city, state, and ZIP code		1 Date of transfer		Statement of Withholding on Dispositions by Foreign Persons of U.S. Real Property Interests OMB No. 1545-0902	
		2 Federal income tax withheld			
Withholding agent's Federal identification number	Identification number of foreign person subject to withholding (see instructions)	3 Amount realized	4 Gain recognized by foreign corporation	Copy A For Internal Revenue Service Center For Privacy Act and Paperwork Reduction Act Notice, see the Instructions for Form 8288.	
Name of person subject to withholding		5 Description of property transferred			
Foreign address (number, street, and apt. or suite no.)		6 Person subject to withholding is: An individual <input type="checkbox"/> A corporation <input type="checkbox"/> Other (specify) ▶			
City, province or state, postal code, and country (not U.S.)	7 Country code	Mailing address of person subject to withholding (if different)			

Form **8288-A** (Rev. 2-2016) Cat. No. 62261L **Attach Copies A and B to Form 8288** Department of the Treasury - Internal Revenue Service



Buyer's Duties

- Submit
 - Forms and
 - Withheld funds to IRS



Buyer's Liabilities



- Buyer/Withholding Agent – Liability
 - Penalties for late filing
 - Penalty up to amount withheld for failure to collect
 - Liability for penalties up to \$10,000 and possible imprisonment

Do Realtors® Have Liability?

- Represent buyer or seller
 - Advise:
 - Planning
 - Arranging
 - Consummation



Do Realtors® Have Liability?

- Yes
 - Seller says he will lie about being foreign to avoid withholding
 - Must give notice
 - In writing
 - Not to rely on statements and/or certifications by seller
 - Then NO liability
- Failure to notify
 - Liability up to the amount of funds received in the transaction

Is Withholding Required For A Short Sale Or When The Seller Is Receiving No Money?

- Yes
 - Withholding is calculated from the contract price (generally)
 - Check your sales contract may have a provision for such a situation

(iv) In the event the net proceeds due Seller are not sufficient to meet the withholding requirement(s) in this transaction, Seller shall deliver to Buyer, at Closing, the additional COLLECTED funds necessary to satisfy the applicable requirement and thereafter Buyer shall timely remit said funds to the IRS or escrow the funds for disbursement in accordance with the final determination of the IRS, as applicable.

Seller Has No Money!

- Short sale
 - No automatic reduction
 - May apply for Withholding Certificate

Form **8288-B**
(Rev. February 2016)
Department of the Treasury
Internal Revenue Service

Application for Withholding Certificate for Dispositions by Foreign Persons of U.S. Real Property Interests

OMB No. 1545-1060

► Please type or print.

Withholding Certificate Application

- Seller or Buyer applies and receives Withholding Certificate
 - Reduce amount of withholding
 - Eliminate required withholding
 - Can be denied



Withholding Certificate Application

- Apply soon
 - Coordinate with closing agent
 - No later than day of closing
- IRS can be slow to respond



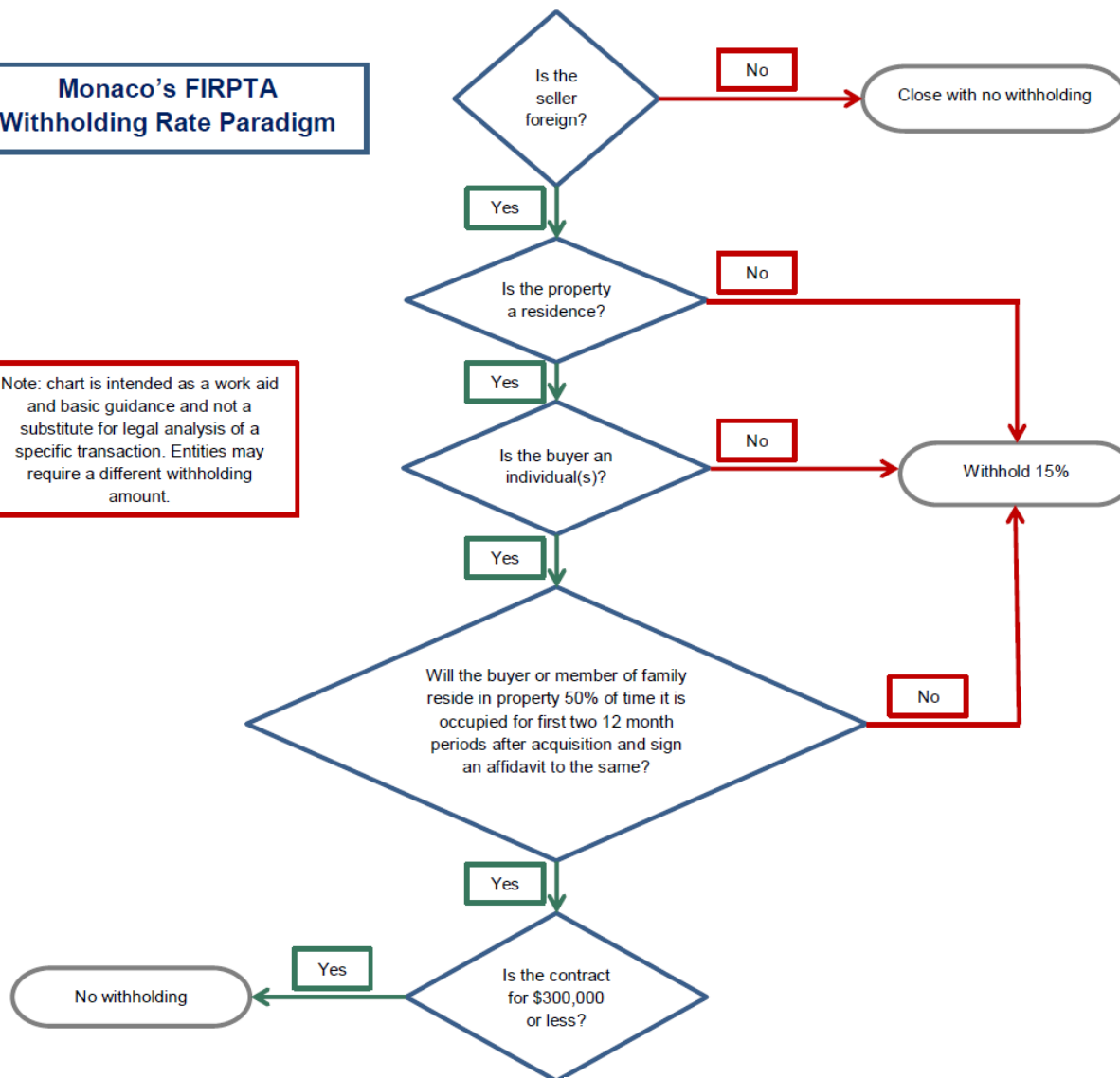
Are There Exemptions?

- Yes
- Sale price \$300,000 or less
 - Residence
 - Individual(s) to take title
 - Buyer or family member will reside in property
 - Minimum 50% of time occupied
 - First two 12 month periods post acquisition



Monaco's FIRPTA Withholding Rate Paradigm

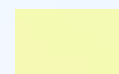
Note: chart is intended as a work aid and basic guidance and not a substitute for legal analysis of a specific transaction. Entities may require a different withholding amount.



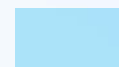
More Details Exemption Requirements

- Limited use needs to pass 50% test
 - Do not count vacant days in 50% test
- Can use if family member to occupy

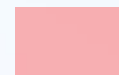
January	February	March	April
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Mr. & Mrs. Buyer



Buyer's Son



Rental



Vacant

More Details Exemption Requirements

- Buyers must sign an affidavit, under penalties of perjury that they (buyers) meet the requirements of the exemption
- If buyers do not comply with occupancy after sale, buyer could be liable for 15% of sale price, plus penalties and interest to the IRS



More Details Exemption Requirements

- Cannot be
 - Vacant land
 - “Teardown”
 - Company purchase
 - Commercial property
- IRS gives caution against pressure on buyer to sign affidavit



If Qualified For \$300,000 Exemption, Withholding Rate Is 0%



Seller Will Need To File A Tax Return



What Has Changed?

New Rate



Did Change Effect The \$300,000 Exemption?

- No
- Did not change how to qualify for the \$300,000 exemption



New Reduced Withholding Rate!

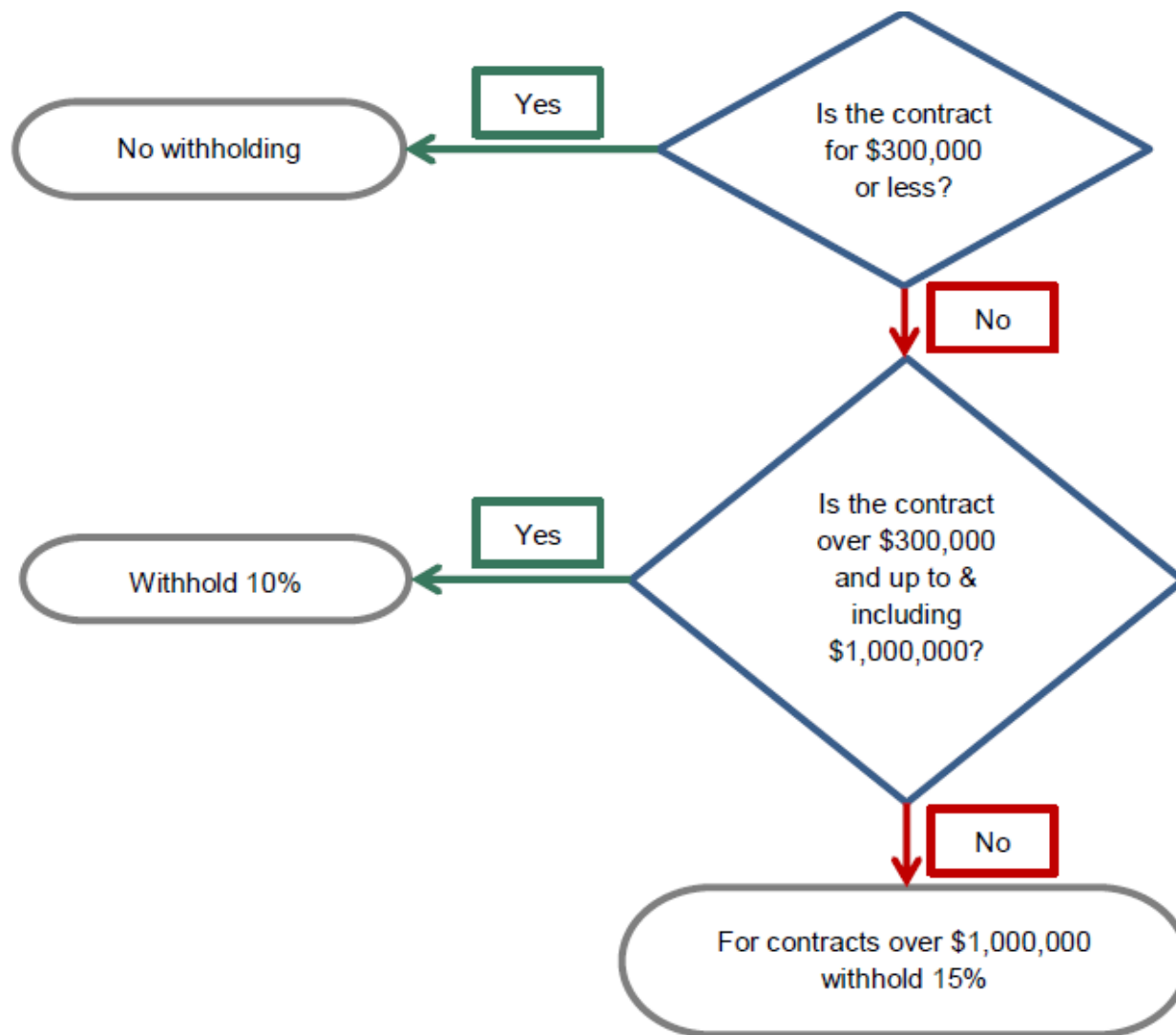
- Sale amount over \$300,000 and
- Sale amount up to and including \$1,000,000
 - May qualify for reduced rate of 10% withholding



How To Qualify For Reduced Rate?

- Residence
- Individual(s) to take title
- Buyer or family member will reside in property
 - Minimum 50% of time occupied
 - First two 12 month periods post acquisition

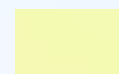




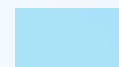
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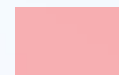
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- If buyers do not comply with occupancy after sale, buyer could be liable for 15% of sale price, plus penalties and interest to the IRS



More Details Exemption Requirements

- Cannot be
 - Vacant land
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 - Company purchase
 - Commercial property
- IRS gives caution against pressure on buyer to sign affidavit



If Qualified For Reduced Withholding Rate Is 10%

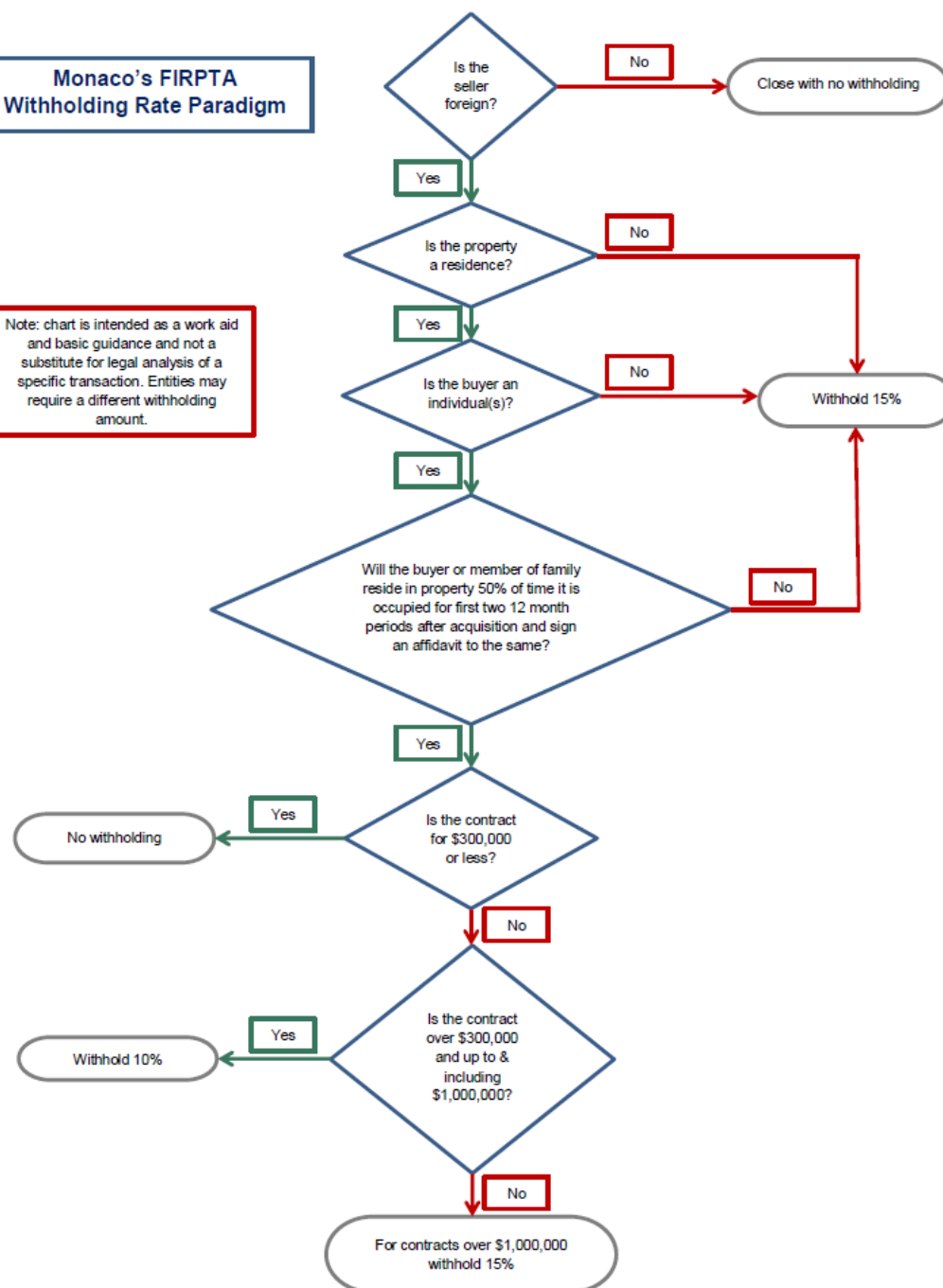


Seller Will Need To File A Tax Return



Monaco's FIRPTA Withholding Rate Paradigm

Note: chart is intended as a work aid and basic guidance and not a substitute for legal analysis of a specific transaction. Entities may require a different withholding amount.



For Smooth Closings

- Find out early if seller is foreign – always ask
- Inform settlement agent and buyer of seller's foreign status
- Inform foreign seller of the required 15% withholding
- Use the \$300,000 exception carefully
- Use the \$1,000,000 reduced rate carefully
- Close on time and
- Be happy!



Questions?