

2023 FLORIDA SEMINAR

# FIRPTA

The Basics & Beyond



**TOTAL FIRPTA**  
 LLC  
 A SIMPLE APPROACH TO A COMPLICATED TAX MATTER



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# INTRODUCTION

The tax code relating to FIRPTA is vast and wide. It applies to many types of transactions, not just real estate. It is critical for title agents to have a foundational understanding of FIRPTA, for many reasons:

1. The decisions we make in our offices can adversely affect buyers by creating IRS penalties.
2. The way FIRPTA is handled can directly impact a seller's ability to get a refund.
3. To save relationships, penalties are absorbed, which hurts your bottom line.
4. Repeat offenses could impact your relationship with your underwriter.
5. Conversely, knowing how to handle FIRPTA transactions well, could be a factor in growing your business in a stagnant or declining market.

*If you don't like something, change it. If you can't change it, change your attitude.*  
– Maya Angelou



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# WHAT IS FIRPTA?

- FIRPTA is an acronym that stands for the Foreign Investment in Real Property Tax Act of 1980. It was designed to even the playing field between foreign and domestic investors.
- FIRPTA requires that when a foreign seller (a “transferor”) transfers U.S. real property, a certain percentage of the money realized by that transferor must be withheld and remitted to the Internal Revenue Service (IRS). This withholding, which is the obligation of the buyer (the “transferee”), serves to preemptively collect U.S. taxes that may be owed by the transferor. While withholding will not be required in every sale of U.S. real property by a foreign transferor, settlement agents should assume that FIRPTA applies to **every** transfer unless an exemption applies.



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# WHAT IS FIRPTA?

FIRPTA is a withholding tax, not a payable income tax, which means the excess tax is refundable:

INCOME TAX	VS	WITHHOLDING TAX
<ul style="list-style-type: none"><li>- Actual, permanent, nonrefundable</li><li>- Paid by the receiver of the income (aka Seller)</li><li>- You owe it, you pay it, it's gone forever!</li></ul>	.	<ul style="list-style-type: none"><li>- Estimated, temporary, refundable</li><li>- Paid by the payer of the income (aka Buyer)</li><li>- You pay it, might not owe it, might get a refund.</li></ul>



# WHAT IS FIRPTA?

Abstract United		Jamaica, NY. 11433, USA		EARNINGS STATEMENTS		
Johnny Bravo			#12341231			
SSN	PAY PERIOD		PAY DATE	EMPLOYEE #		
***-**-5645	03/28/2018 - 04/03/2018		04/04/2018	3214		
INCOME	RATE	HOURS	CURRENT TOTAL	DEDUCTIONS	TOTAL	YTD TOTAL
GROSS EARNINGS	15	40	600.00	FICA - MEDICARE	8.70	121.80
				FICA - SOCIAL SECURITY	37.20	520.80
				FEDERAL TAX	75.10	1,051.41
				STATE TAX	30.00	420.00
<b>YTD GROSS</b>	<b>YTD DEDUCTIONS</b>	<b>YTD NET PAY</b>	<b>TOTAL</b>	<b>DEDUCTIONS</b>	<b>NET PAY</b>	
8,400.00	2,114.01	6,285.99	600.00	151.00	449.00	

➔ The federal income tax system is a pay-as-you-go tax system

➔ Tax is paid as it is earned



# HOW MUCH IS WITHHELD?

FIRPTA requires the buyer to withhold up to 15% of the amount realized.

The amount realized is the sum of:

- The cash paid or to be paid;
- The fair market value of other property transferred, or to be transferred; and
- The amount of any liability assumed by the transferee or to which the property is subject immediately before and after the transfer.

Note: For typical real estate transactions, the amount realized is the contract price (or gross sales price); it is NOT the transferor's proceeds.

## **ASSIGNMENTS OF CONTRACT:**

Withholding under IRC 1445 is applicable when a foreign person assigns their right to purchase a USRPI to another party. For example, if a foreign person signs a contract to buy a house from a builder for \$400,000 but assigns their right to purchase the house for \$30,000 to another individual, that individual is required to withhold \$4,500 (15% of the of \$30,000) on the amount realized by the foreign person.





# HOW MUCH IS WITHHELD?

Note: The amount realized cannot be allocated entirely to one transferor when two or more transferors own the USRPI.

If one or more foreign persons and one or more U.S. persons jointly transfer a U.S. real property interest, you must determine the amount subject to withholding in the following manner.

1. Allocate the amount realized from the transfer among the transferors based on their capital contribution to the property. For this purpose, a husband and wife are treated as having contributed 50% each.
2. Withhold on the total amount allocated to foreign transferors.
3. Credit the amount withheld among the foreign transferors as they mutually agree. The transferors must request that the withholding be credited as agreed upon by the 10th day after the date of transfer. If no agreement is reached, credit them equally.



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# WHAT IS REAL PROPERTY?

FIRPTA applies to the sale of REAL PROPERTY by a foreign person. A U.S. real property interest is an interest, other than as a creditor, in real property located in the United States or the U.S. Virgin Islands. Examples include:

- Buildings (houses, condos, commercial, etc.)
- Time Shares/Co-ops
- Deeded parking spaces, docks, boat slips
- Options
- Land and unsevered natural products of the land
- Mines
- Growing crops/Standing Timber
- Swimming pools
- Wells and other natural deposits before extraction
- Fences
- Advertising display
- Leaseholds
- Oil and gas pipelines
- Permanently installed telephone and television cables
- Certain personal property that is associated with the use of real property (such as farming machinery).



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## United States Persons:

- A US citizen
- A US resident
- A domestic partnership
- A domestic corporation
- Any estate other than a foreign estate
- Any trust other than a foreign trust
- Any other person that is not a foreign person

## Foreign Persons:

- Non-resident alien individual
- Foreign corporation that has not made an election to be treated as a domestic corporation
- Foreign partnership
- Foreign trust
- Foreign estate

# WHO'S CONSIDERED FORGEIGN?

Note: A resident alien is NOT a foreign person.

Note: An individual who has a U.S. Social Security number is still considered a Foreign Person if he/she does not have a green card or does not meet the substantial presence test.



# WHAT IS A RESIDENT ALIEN?

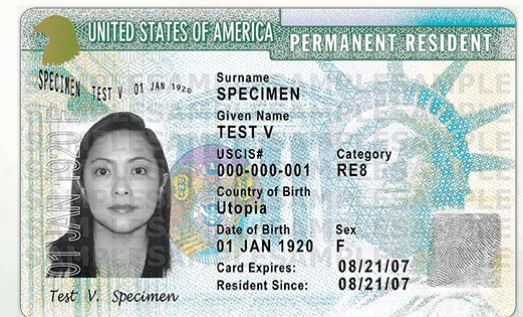
If you are not a U.S. Citizen, you can still be considered a resident alien if you meet **one** of two tests:

## #1 - The Green Card Test

You are a lawful permanent resident of the United States, at any time, if you have been given the privilege, according to the immigration laws, of residing permanently in the United States as an immigrant. You generally have this status if the U.S. Citizenship and immigration services (USCIS) issued you an alien registration card, form I-551, also known as a "green card."

You continue to have U.S. Resident status, under this test, unless:

- You voluntarily renounce and abandon this status in writing to the USCIS,
- Your immigrant status is administratively terminated by the USCIS, or
- Your immigrant status is judicially terminated by a U.S. Federal court.



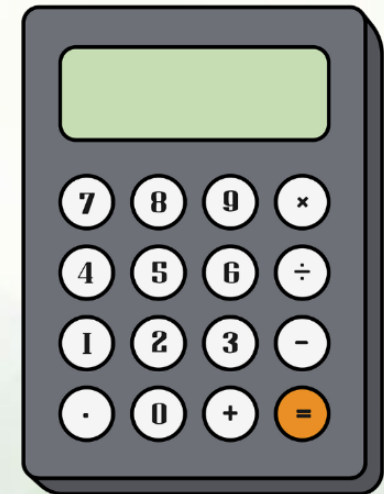


# WHAT IS A RESIDENT ALIEN?

## #2 - The Substantial Presence Test (SPT)

You will be considered a United States resident for tax purposes if you meet the substantial presence test for the calendar year. To meet this test, you must be physically present in the United States (U.S.) On at least 31 days during the current year, and 183 days during the 3-year period that includes the current year and the 2 years immediately before that, counting:

- All the days you were present in the current year, and
- 1/3 of the days you were present in the first year before the current year, and
- 1/6 of the days you were present in the second year before the current year.





# SUBSTANTIAL PRESENCE TEST

You are treated as present in the US on any day you are physically present in the country, at any time during the day. However, there are exceptions to this rule where certain days are not counted for the substantial presence test:

1. Days you commute to work in the U.S. from a residence in Canada or Mexico if you regularly commute from Canada or Mexico.
2. Days you are in the U.S. for less than 24 hours, when you are in transit between two places outside the United States.
3. Days you are in the U.S. as a crew member of a foreign vessel.
4. Days you are unable to leave the U.S. because of a medical condition that develops while you are in the United States.
5. Days you are an exempt individual:
  - Foreign government-related individual under A (except A-3) or G (except G-5)
  - Teacher or trainee under J or Q visa (for first 2 years)
  - Student under an F, J, M, Q visa (for first 5 years)
  - Professional athlete temporarily in the U.S. for a charitable sports event.



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# SUBSTANTIAL PRESENCE TEST EXAMPLE

Ask these questions first:

1. Has this seller been in the US for at least 31 days this year? If yes, go to next question.
2. Is this seller an exempt individual? If no, then proceed to count the days.

Many sellers are in the US for an average of 135 Days per year:

- $135 \text{ Days} \times 100\% = 135 \text{ Days (2023)}$
- $135 \text{ Days} \times .3333\% = 45 \text{ Days (2022)}$
- $135 \text{ Days} \times .1666\% = 23 \text{ Days (2021)}$
- Total Days for SPT = 203 Days



# RESIDENT ALIENS: OTHER CONSIDERATIONS

In some cases, you are allowed to make elections which override the green card test and the substantial presence test:

- First-Year Choice To Be Treated as a Resident
- Nonresident Spouse Treated as a Resident
- Closer Connection To a Foreign Country (Form 8840)
- Tax Treaties

Also, you can be both a nonresident and a resident during the same year. This usually only happens during arrival and departure years. This is known as a dual-status alien.

Note: Dual status alien is not the same as dual citizen.

Dual Status = residency status changes during the year

Dual Citizen = citizen of more than one country



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# LIMITED LIABILITY COMPANIES

SINGLE-MEMBER LLC	MULTI-MEMBER LLC	LLC MADE AN ELECTION TO BE TREATED AS A CORPORATION
Default classification is:	Default classification:	Now classified as:
Disregarded Entity	Partnership	C-Corporation
Look to the owner of the LLC	Look to the LLC itself	Look to the corporation itself
EIN not required	Usually has an EIN	Usually has an EIN
Files on individual return (1040 or 1040NR)	Files a partnership return (Form 1065)	Files a corporate return (Form 1120)
FIRPTA if owner is foreign**	No FIRPTA	No FIRPTA

\*\*Instructions for Form 8288: A disregarded entity cannot be the transferor for purposes of section 1445. Instead, the person considered as owning the assets of the disregarded entity for federal tax purposes is regarded as the transferor. A disregarded entity for these purposes means an entity that is disregarded as an entity separate from its owner.



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# US TRUST OF FOREIGN TRUST

The tax status of a trust depends on two tests:

A trust that does not meet both the court test **and** the control test is considered a foreign trust.

TEST #1 – The Court Test	TEST #2 – The Control Test
A court within the United States is able to exercise primary supervision over the administration of the trust.	One or more United States persons have the authority to control all substantial decisions of the trust with no other person having the power to veto any of the substantial decisions.



# SELLER OPTIONS

Assuming the parties agree, foreign sellers typically have 2 options when it comes to FIRPTA.

**OPTION #1:** The withholding (10% or 15%) is collected from the seller's proceeds and sent directly to the IRS after closing using forms 8288 and 8288A.

- Seller will need to have a US tax ID number to get a “receipt” for the withholding from the IRS.
- Seller will need to file a tax return and attach the receipt to claim a refund of overpaid withholding.
- Funds must be remitted to the IRS within 20 days of the closing. After the 20th day, the buyer will be assessed the following:
  - Failure to Pay = Withholding Amount x .50% x number of months late
  - Failure to File = Withholding Amount x 4.5% x number of months late (5 max)
  - Interest = Withholding Amount + Penalties x Current Interest Rate (compounding daily)
- Once remitted, provide all parties with redacted copies of the forms, check, and tracking number.

**PRO TIP:** On the check, reference the type of withholding, the accounting period, and the buyer's TIN. For example, if the closing took place July 6, 2023, and the buyer's SSN was 555-44-6666, you would write/type “8288/July 2023/555-44-6666” in the memo section on the face of the check.



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# SELLER OPTIONS

**OPTION #2:** The withholding (10% or 15%) is collected from seller's proceeds and retained in escrow pending the IRS's determination. This certificate can be applied for by the buyer or the seller and shows a calculation of the seller's gain on the sale and potential tax owed.

- The seller must notify the buyer in writing that they have applied for a withholding certificate.
- Only form 8288-B is used. This form (along with supporting documents) must be postmarked on or before the date of transfer.
- All parties will need to have (or be willing to apply for) a US tax ID number.
- The withholding must be reduced by 10% or more to be considered.
- When IRS responds, only the reduced amount needs to be submitted within 20 days of the date shown on the certificate. The balance of the escrow account can be released back to the seller. Current processing time as of July 2023 is 12 months or more.
- Seller will need to file a tax return and may be eligible for an additional refund of any overpaid withholding.

**PRO TIP:** Be sure to use the most current version of Form 8288 & 8288A when remitting funds after a withholding certificate and always include a copy of the certificate with the submission.



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# EXCEPTIONS TO FIRPTA

According to IRS.gov, there are several exceptions to FIRPTA. The most common ones, that we encounter in real estate transactions, are:

1. Transferor in Not a Foreign Person: See Seller Exception
2. Purchase of Personal Residence for \$300,000 or Less: See Buyer Exception
3. Government Buyer: Property acquired by the United States, a US state or possession, a political subdivision, or the District of Columbia.
4. No Consideration Paid: The Amount Realized by the transferor is zero (for example, the property is transferred as a gift and the recipient does not assume any liabilities or furnish any other consideration to the transferor).
5. Non-Recognition of Gain: Seller gives written notice that they are not required to recognize any gain on the sale due to a nonrecognition provision in the Code or a tax treaty.
6. Withholding Certificate Issued by the IRS: See Withholding Certificate



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# “SELLER” EXCEPTIONS

No withholding is required for FIRPTA if the transferor of a U.S. real property interest is not a foreign person:

- The transferor can provide a Certification of Non-Foreign Status (CNFS) to the transferee to inform them that withholding is not required. To be valid, the CNFS must:
  1. Be signed under penalty of perjury by the transferor,
  2. State the transferor is not a foreign person or entity, and
  3. Contain the transferor's name, address, and US tax ID number
- A transferee that obtains such a certification must retain that document for five years.
- Unless the CNFS is known to be (or is suspected of being) false, obtaining this certification excuses the transferee from any liability otherwise imposed by section 1445 and § 1.1445-1(e).
- The rules do not impose any obligation upon a transferee to obtain a certification from the transferor, thus, a transferee may instead rely upon other means to ascertain the non-foreign status of the transferor. If, however, the transferee relies upon other means and the transferor was, in fact, a foreign person, then the transferee is subject to the liability imposed by section 1445 and § 1.1445-1(e).



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# “SELLER” EXCEPTIONS

Every individual transferor, an authorized officer of a corporate transferor, a general partner of a partnership transferor, or the trustee, executor, or fiduciary of a trust or estate transferor, must sign the CNFS. If they are not able to sign, that may indicate they are foreign.

A foreign corporation electing to be treated as a domestic corporation must also attach a copy of the IRS acknowledgment of such election (which must state that the information required by CFR Section 1.897-3 has been determined to be complete) to the CNFS; the CNFS cannot be relied upon if the IRS acknowledgment is not attached.

A “disregarded entity” can not sign the CNFS since it is not treated as the transferor. With a disregarded entity, the IRS instead looks directly to the individual owner (e.g., the single member of an LLC) as the actual taxpayer and transferor. The owner of the disregarded entity must sign the CNFS. If the owner of a disregarded entity is a Foreign Person, this exemption does not apply.

Instead of delivering the CNFS to the transferee, the transferor may deliver it to a Qualified Substitute, such as a settlement agent. The Qualified Substitute will then provide the transferee with a Qualified Substitute statement (“QSS”), signed under penalties of perjury, indicating that the CNFS is in the Qualified Substitute’s possession. The QSS may also be relied upon unless the Qualified Substitute has reason to believe the CNFS is false.



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# BUYER EXCEPTIONS

No withholding is required under section 1445(a) if one or more individual transferees acquire a U.S. real property interest for use as a residence and the amount realized on the transaction is \$300,000 or less. To utilize this exception:

- Buyer must be an individual – not a trust, corporation, etc.
- Buyer must have definite plans to reside at the property for at least 50 percent of the number of days that the property is used by any person during each of the first two 12-month periods following the date of the transfer.
- Buyer's family includes only his brothers and sisters (whole or half-blood) spouse, ancestors, and lineal descendants

If buyer does not maintain minimum number of days, they could be liable for the tax unless they could establish that the failure was caused by a change of circumstances that could not be reasonable anticipated at the time of sale.

Although IRS does not require a form to be filed, have buyers sign affidavit!

If the above applies but the sales price is \$300,001 - \$1,000,000 withholding is reduced to 10%

Note: if the seller does not already have an ITIN for 1099 reporting, they will not be able to apply for one if the withholding is eliminated due to this exception.



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# NON-RECOGNITION OF GAIN OR LOSS

- The transferee may receive a notice from the transferor signed under penalties of perjury stating that the transferor is not required to recognize gain or loss on the transfer because of a non-recognition provision of the Internal Revenue Code. The transferee may rely on the transferor's notice unless only part of the gain qualifies for non-recognition, or the transferee knows or has reason to know that the transferor is not entitled to the claimed non-recognition.
- There is a misconception that a 1031 Exchange falls under the non-recognition provisions mentioned above. However, the seller utilizing a 1031 Exchange does not automatically exempt the sale from FIRPTA. This type of exception does not apply to FIRPTA unless:
  - A. The sale includes a simultaneous closing, and
  - B. The exchange is a complete exchange - THERE CAN BE NO BOOT!
- If a simultaneous 1031 exchange occurs, the seller must provide a detailed notice to the buyer explaining why there is no gain. Then by the 20th day after the date of transfer, the buyer must:
  - A. Mail a copy of the seller's notice to the IRS, and
  - B. Include a cover sheet that includes their name, tax ID number, and address.



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# NON-RECOGNITION OF GAIN OR LOSS

If a simultaneous closing is not an option, or if the simultaneous closing does not result in a complete exchange, the seller will have to make a choice:

1. Allow the withholding to be sent to IRS and pay capital gains tax on it, or
2. Fund the withholding personally so it's not considered boot once tax refund is received from the IRS.



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# WITHHOLDING CERTIFICATE

An IRS withholding certificate may be relied upon to reduce or eliminate withholding under FIRPTA. The certificate may be issued if:

- A. Reduced withholding is appropriate because the 10% or 15% withholding amount (as applicable) exceeds the transferor's maximum tax liability;
- B. The transferor is exempt from U.S. tax, or non-recognition provisions apply; or
- C. The transferee or transferor enters into an agreement with the IRS for the payment of the tax.

If approved before closing – the buyer is only required to withhold the lower amount.

If approved after closing – the funds can be placed in escrow and then disbursed once the certificate is received.

**PRO TIP:** Refer to the purchase and sale contract to learn if the buyer must agree to hold funds in escrow.



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# BEST PRACTICES

FIRPTA is a very complicated area and is best left to tax professionals. Here are some helpful tips for settlement agents:

## **DON'T:**

1. Accept closing or other instructions that require you to determine whether FIRPTA applies, or to act as Withholding Agent, unless you understand those obligations;
2. Determine whether a seller meets the “substantial presence” test to be considered non-foreign;
3. Determine whether a buyer qualifies for the Residence exemption;
4. Sign any FIRPTA forms, including those being sent to the IRS, as “Withholding Agent” unless that is your intention, and you understand the ramifications of acting in this capacity;
5. Rely on any documents you know (or think) may be false, misleading, or incomplete;
6. Attempt to explain any laws or regulations related to FIRPTA;
7. Agree to escrow withheld monies while waiting for the seller to provide documentation evidencing an exemption; or
8. Charge an additional or separate fee for FIRPTA-related matters.



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# BEST PRACTICES

## DO:

1. Assume FIRPTA applies to every transaction involving a foreign seller and encourage the seller and buyer to seek professional FIRPTA advice;
2. If relying on a FIRPTA exemption, document your closing file with evidence supporting that exemption; and
3. If you've agreed to assist with the remittance of FIRPTA monies and forms to the IRS, including acting as a Qualified Substitute, make sure you understand your role and obligations and that monies and forms are properly remitted to the IRS no later than the 20th day after the closing.
4. Establish a standard operating procedure when dealing with FIRPTA transactions.
5. Encourage foreign sellers to work with a FIRPTA expert as early as possible.



# Thank You!



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