



FIRPTA Withholding Rate Increased to 15%

Effective Feb. 16th, 2016, Withholding Agents (Buyers) will need to start holding back more proceeds from the sale of property by a foreign person due to recent changes to the Foreign Investment in Real Property Tax Act (FIRPTA).

The changes were part of the year-end tax extension legislation signed into law by President Obama on Dec. 18, 2015. (Reference: The legislation is H.R. R. 2029, now known as Public Law 114-113. See Section 324 for text of changes.)

FIRPTA is a tax law passed in 1981 requiring purchasers of property to withhold and remit a portion of the sales price to the IRS unless an exception applies. requiring foreign persons to pay U.S. income tax on the gains they make from selling U.S. real estate. The duty is on the buyer (and not the settlement agent) to deduct and withhold a portion of the sales price and report the sale to the IRS withhold a portion of the sales price and remit to the IRS. In some situations a buyer or seller can apply for a withholding certificate to reduce the withholding amount. Buyers can withhold less than the statutory amount if they obtain a determination of the specific amount of tax owed by the foreign national using IRS Form 8288-B. In most cases, the settlement agent is the party that actually remits the funds to the IRS, but the buyer is held legally responsible. Additionally, until the tax is paid in full, the government may obtain a security interest in the real property. Per the IRS regulations, the buyer or transferee is legally responsible for any withholding due.

Under the changes, the base withholding rate for sales by foreign nationals will increase to 15% of the total sales price (up from the current 10%). The changes do not impact the 10 current FIRPTA exceptions listed in Publication 515, including the exception for sales under \$300,000 where the buyer intends on using the property as a residence. For a detailed explanation of this exception and whether this may apply please see Publication 515 or talk with your tax professional. Additionally the current 10% withholding amount still applies to sales of primary residences where the sales price is less than \$1 million.

The formula, if none of the 10 exceptions apply:

- If the amount realized (generally the sales price) is \$300,000 or less, and the property will be used by the buyer as a primary residence, the withholding rate is 0%.
- If the sale price is \$300,000 or less, and the property will not be used as a principal residence, the withholding rate is 15% of the sale price
- If the sale price is greater than \$300,000 and not over \$1 million, and the buyer intends to use the property as their primary residence the withholding rate is 10% of the sale price
- If the sale price is greater than \$300,000 and not over \$1 million, and the buyer does not intend to use the property as their primary residence the withholding rate is 15% of the sale price
- If the amount realized exceeds \$1 million, then the withholding rate is 15% on the entire amount, regardless of use by the buyer.

It is a good assumption that the risks associated with using the \$300,000 exemption will continue and expand to the new rate for transactions under \$1 million. Buyers looking to take advantage of the exemption should document (under the penalty of perjury) the buyer's intent to use the property as a residence. It is also a good idea to be on the lookout for red flags related foreign sellers forcing the buyer to agree to claim residence status merely to lower the withholding rate. A buyer that fails to comply appropriately with FIRPTA could be liable for any additional withholding tax, penalty and interest. We recommend any buyer or seller should contact a tax professional or see Publication 515 found at www.irs.gov for more information.

Source: American Land Title Association. Information contained herein is for reference purpose only. Please always consult with your attorney.