

# American Fidelity Titles' Insider's Edition

## American Fidelity Title

### Tax Information for Foreign Owners of U.S. Real Estate

With the increasing globalization of trade and investments, foreign ownership of U.S. real estate continues to grow. Consequently, U.S. Realtors and rental agents/property managers are encountering an increasing number of situations that involve foreign persons acquiring U.S. real estate as part-time residences, for investment or in some cases to conduct a U.S. business. The U.S. tax rules that apply to ownership and dispositions of U.S. real estate by foreign persons are different in some important respects from the rules that apply to U.S. persons.

**Definition of Foreign Persons** – Because a number of U.S. federal tax rules differ when a foreign person is involved or apply only to foreign persons, it is important for a U.S. real estate professional to understand when an individual or entity is considered foreign for U.S. federal income or estate tax purposes. A nonresident alien is defined **for federal income tax purposes** as an individual who is neither a U.S. citizen nor a resident of the United States within the meaning of Internal Revenue Code. An alien individual is a resident of the U.S. for federal income tax purposes if he or she meets either of the two tests under code sec 7701(b).

The first test is the “**green card**” test. If an alien has been admitted for U.S. permanent residences (i.e., has a green card) at any time during the calendar year, the alien is a resident of the United States and is taxed on his or her worldwide income, the same as a U.S. citizen. Otherwise, the U.S. immigration status generally is not controlling or relevant for U.S. federal tax purposes. In this respect, the U.S. differs from many foreign countries, in which immigration and tax status are integrated, a difference that frequently causes confusion.

The second test is the **substantial presence test**. Under the substantial presence test, an alien individual is a resident for the U.S. federal tax purposes if the alien is physically present in the U.S. for 183 days or more during the current calendar year. Alternatively, if the alien is physically present for at least 31 days during the current year, the alien may be treated as a U.S. tax resident *in the current year* under a three-year look-back test in which each day of presence in the current year is counted as a full day, each day of presence in the first preceding year is counted as one-third of a day, and each day of presence in the second preceding year is counted as one-sixth of a day. If the total of such days is 183 days or more, the alien *may* be a U.S. tax resident *for the current year* unless certain exceptions apply and the alien files certain required information with the IRS to claim the benefit of any relevant exception. As with the green card test, if an alien is a U.S. tax resident under either version of the substantial presence test, the alien is taxed on his or her worldwide income, the same as a U.S. citizen.

**The Foreign Investment in real Property Tax Act** – Code Sec. 897 provides rules for the taxation of nonresident alien individuals and foreign corporations on sales or other dispositions of U.S. real property interests (including installment sales, exchanges, foreclosures, and deeds in lieu of foreclosure of a U.S. real property interest) FIRPTA applies to what it defines as a U.S. real property interest, which includes not only interest in land, but interests in buildings, mines wells, crops and timber as well. Because Congress was concerned that foreign persons would try to avoid FIRPTA by incorporating their U.S. real estate holdings, a U.S.

real property interest is defined to also include any interest in a U.S. corporation if that U.S. corporation is a “U.S. real property holding company” with the result that a disposition of its stock by a foreign investor may be subject to federal income tax under FIRPTA. A U.S. corporation is a U.S. real property holding company if the fair market value of its U.S. real property interests equals 50 percent or more of the sum of the fair market value of its U.S. real property interests, interests in real property located outside of the United States, and trade or business assets. A foreign corporation may also be classified as a U.S. real property holding company, but the sale of stock in a foreign corporation by a foreign person generally is not subject to U.S. federal income tax.

Since 1985, a disposition of a U.S. real property interest by a foreign corporation or nonresident alien individual generally is subject to a withholding tax regime under Sec 1445 of the code. **Under the withholding tax regime, any purchaser of a U.S. real property interest from a foreign seller must withhold 10 percent of the gross purchase price and remit such amount to the IRS within 20 days of the closing. The purchase price includes cash plus the fair market value of any other property transferred to acquire the real estate. A purchaser failing to withhold is liable for any uncollected withholding tax, as well as penalties and interest charges.**

Attorneys Title Insurance Fund



*Amy E. Stark*  
Chief Operating Officer

As we witness the changing marketplace, we are finding foreign sellers and buyers more frequently in residential real estate transactions.

Since we receive many questions about this subject, I thought it would be beneficial to provide you with a general overview that may help in answering some of the questions you have.

Should you have **any** specific file questions, please know you can always call us for assistance.

Regards,

*Amy*

**“All things being equal, people want to do business with their friends. All things being not quite so equal, people STILL want to do business with their friends.”**

“If you make a sale, you can earn a commission. If you make a friend, you can earn a fortune”. Those in sales who employ this philosophy are the top performers and the top paid salespeople. They build relationships. They don't worry about their quotas. They concentrate on the value they provide to their customers and corresponding orders that accompany it. I challenge you that this is the single most powerful and most financially rewarding lesson.

Jeffrey Gitomer, “Little Red Book of Selling”  
Referred by Jim Dennis, The Addison Mortgage Group

For more information, please contact your American Fidelity Title Marketing Representative at 954-492-5000

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The information contained herein is not intended to be legal or accounting advice.

### Things that make you go “Hmmm”

Everyday more money is printed for the board game “Monopoly” than for the US Treasury

Many years ago in Scotland a new game was invented.  
It was ruled “Gentleman Only...Ladies Forbidden”...  
& thus the word “GOLF” was entered into the English Language.

It is impossible to lick your elbow . (But whatever you do, don't try it)

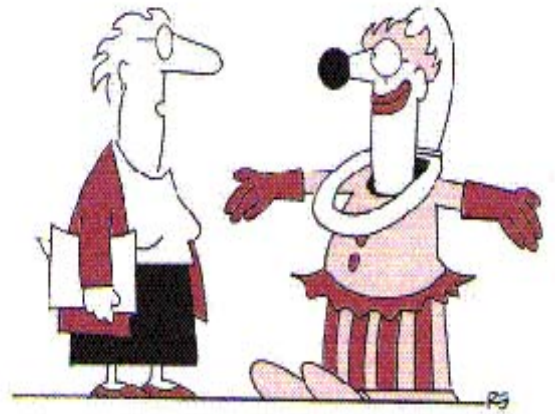
The state with the highest percentage of people who walk to work every day: Alaska

The 1<sup>st</sup> novel ever written completely on a typewriter was “Tom Sawyer” by Mark Twain.

The cost of raising a medium-size dog to the age of 11: \$6400

And Finally....

At least 75% of the people who read this tried to lick their elbow.




**“Just because it sells burgers, I'm not sure ‘Ronald McToilet’ is the best way to sell industrial plumbing supplies”**

Jeffrey Gitomer

# American Fidelity Title

*Providing premier Closing & Title Services*

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" Achievement is not when you complete what you wanted to do, but when you accomplish what you dreamed of doing."

John Glueck