



AbdulJaami, PLLC

International Commercial Transactions

Foreigners and U.S. Real Estate

Impact of U.S. Taxes

Federal and New York State and City



AbdulJaami, PLLC

International Commercial Transactions

Saboor H. AbdulJaami

Attorney and Counselor at Law

410 Park Avenue, Suite 1530

New York, NY 10022-4407

Tel: 1.646.435.0668

Fax: 1.646.435.0664

email: sabduljaami@shajlaw.com

web address: www.shajlaw.com



Foreigners and U.S. Residency

- Determining U.S. residency
 - Person
 - **Green Card test:** green card holders are taxed as U.S. residents
 - In a particular year, non-U.S. residents who have lived in the U.S. for at least 183 days are subject to U.S. taxation
 - **Substantial Presence test:** in a particular year, non-U.S. residents who have been in the U.S. for at least 31 days, should perform the following calculation:
 - (number of days in U.S. during current year) x 1 + (number of days in U.S. during previous year) x (1/3) + (number of days in U.S. two years ago) x (1/6) = ____
 - Example, assuming the current year is 2005 and a non-U.S. resident visited the U.S. for 60 days in 2005, 180 days in 2004, and 90 days in 2003: $60 \times 1 + 180 \times (1/3) + 90 \times (1/6) = \underline{135}$
 - If the total is 183 or more, the non-resident may be treated as a U.S. resident, subject to certain exceptions
 - Entity
 - A corporation that is incorporated outside of the U.S. is a foreign corporation
 - Due to possible “check the box” elections, entities, including foreign corporations, may or may not be treated as being resident in the U.S.



Foreign Investment in Real Property Tax

- Foreign Investment in Real Property Tax Act of 1980 (FIRPTA)
 - Under FIRPTA, gains or losses realized by foreign corporations or non-resident alien individuals (foreigners) from any sale, exchange, or other disposition of a U.S. real property interest are taxed in the same manner as income effectively connected with the conduct of a U.S. trade or business
 - “Income effectively connected with the conduct of a U.S. trade or business” is taxed at the rates that apply to U.S. citizens/resident aliens
 - Individuals: 10-35%
 - Corporations: 15-35%
 - To ensure tax collection, FIRPTA subjects foreign sellers of U.S. real estate to a 10% withholding tax
 - Purchaser is responsible for withholding the tax and must forward the withheld amount to the IRS within 20 days of the sale
 - There is no withholding if the property is purchased for (i) use as a personal residence and (ii) \$300,000 or less
 - A tax treaty may reduce the total tax paid, but usually not below the 10% withholding threshold



Foreign Investment in Real Property Tax

- What constitutes a U.S. real property interest?
 - Physical interests:
 - Land
 - Buildings (including personal residences)
 - Mines, wells and other natural deposits
 - Growing crops and timber
 - Personal property associated with the real estate (hotel fixtures and furniture)
 - Legal interests:
 - Fee ownership
 - Co-ownership
 - Leasehold
 - Options to purchase or lease property
 - Interests in certain domestic corporations
 - Any direct or indirect right to share in the appreciation in value or proceeds from the sale of real property



Foreigner's Sale of Real Estate and Tax

- Sale of property and Withholding
 - Acquirer must deduct and withhold 10% of the property's sale value
 - Persons receiving property through an exchange or property or as a gift are counted as Acquirers
 - Property's sale value is equal to the sum of the following:
 - Cash paid at sale or in the future (interest excluded)
 - Market value of other property ancillary to the deal
 - Assumed liabilities
 - Liabilities that the property was taken subject to
 - If acquirer does not withhold, he/she is liable for any uncollected taxes
 - Reporting
 - Within 20 days of withholding, Acquirer must file [Form 8288](#) and [Form 8288-A](#) and deposit withheld tax
 - Seller may file [Form 8288-B](#) to request reduced or eliminated withholding.



Foreigner's Sale of Real Estate and Tax

- Foreign seller's reporting requirements
 - Necessary forms:
 - Person
 - [Form 1040NR](#)
 - [Schedule D](#)
 - Attach receipted copy of Form 8288-A
 - Corporation
 - [Form 1120-F](#) + Schedules
 - Attach receipted copy of Form 8288-A
 - Additional forms (as applicable):
 - [Form 4797](#) (sale of business property)
 - [Form 6251](#) (alternative minimum tax)
- Foreign seller and U.S. tax identification number
 - Forms 8288, 8288-A and 8288-B require the foreign seller to input a U.S. taxpayer identification number
 - Obtaining an Individual Taxpayer Identification Number (ITIN)
 - ITINs are only issued upon the filing of a U.S. tax return (there are some exceptions)
 - Use [Form W-7](#)



Real Estate Rental Income and Tax

- Varies based on type of income:
 - Business income
 - Income resulting from the operation of a U.S. business (i.e. active management of commercial real estate)
 - Investment income
 - Income not connected with the operation of a business – passive investment income
- Business income
 - Taxed at the rates that apply to U.S. citizens/resident aliens
 - Individuals: 10-35%
 - Corporations: 15-35%
 - Mortgage interest, real property taxes, maintenance, repairs and depreciation can be deducted if one of the following forms is filed:
 - Individuals: file Form [1040NR](#)
 - Corporations: file Form [1120-F](#)



Real Estate Rental Income and Tax

- Investment income
 - Withholding tax: 30% of *gross income*
 - Tax treaties may decrease withholding tax
 - *Gross income* includes all real estate taxes, operating expenses, ground rent, repairs, interest and principal on any existing mortgages, and insurance premiums that owner has lessee pay
 - Forms
 - [1042](#)
 - [1042-S](#)
 - Foreign investors may elect to have their passive investment income treated as business income
 - Provides the ability to offset gross income with deductions (interest expenses, depreciation)
 - The election will apply to all income, including income that would otherwise not be treated as business income
 - The election applies in subsequent years, but may be revoked with the consent of the IRS; 5 year wait before a new election can be made



Real Estate – New York State and City Taxes

- Real Estate Transfer Tax Rates
 - NY State (seller)
 - \$2 per \$500 of consideration
 - NY City (seller)
 - Residential
 - Total consideration \$500,000 or less, 1%
 - Total consideration more than \$500,000, 1.425%
 - Commercial
 - Total consideration \$500,000 or less, 1.425%
 - Total consideration more than \$500,000, 2.625%



Real Estate – New York State and City Taxes

- Real Estate Transfer Tax Rates
 - NY State (buyer)
 - Residential (1, 2, 3 family, condo or coop)
 - Total consideration \$1,000,000 or more, 1%
- Mortgage Recording Tax
 - NY City (buyer)
 - Mortgage securing less than \$500,000, 2%
 - Mortgage (1, 2, 3 family or condo) securing \$500,000 or more, 2.125%
 - All other mortgages (coop, commercial), 2.75%