

WFG Underwriting Bulletin



To: All Policy Issuing Agents of WFG National Title Insurance Company
From: Underwriting Department
Date: February 12, 2016
Bulletin No. NB2016-01
Subject: FIRPTA Withholding Rate to Increase to 15% (up from the current 10%)

Starting **Feb. 16, 2016**, settlement agents will need to start holding back more proceeds from the sale of property by foreign persons 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 1980 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. 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 obtains a security interest in the real property.

Under the changes, the 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 current FIRPTA exemptions including the exemptions for sales under \$300,000 for the sale of primary residence or vacant land. Additionally the current 10% withholding amount still applies to sales of primary residences where the sales price is less than \$1 million.

Summary:

- 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%**. However, as the IRS points out, if the property is not in fact used as a residence, the withholding tax may be collected from the Buyer.¹

- If the amount realized **exceeds \$300,000 but does not exceed \$1 million**, AND the property will be used by the buyer as a **primary residence**, the withholding rate is **10% on the full amount realized**.
- If the amount realized **exceeds \$1 million**, or does not meet the primary residence tests, then the withholding rate is **15% on the entire amount**.

Title and settlement agents will want to review their FIRPTA procedures before the effective date to ensure they will assist the company in compliance with the law. 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 (and their settlement agents) 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. Settlement agents should consider providing a disclosure to the buyer of the legal and tax risk they face for misapplying the exemption. We also urge everyone to be aware of red flags related to foreign sellers possibly 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 held liable for any additional withholding tax, penalty and interest.

Many state and local real estate form contracts contain language specifically referring to a 10% withholding and will likely need to be updated as a result of this change.

It is sometimes difficult to know if FIRPTA withholding requirements apply in a transaction so you may consider obtaining a FIRPTA Affidavit and Certification of Non-Foreign Status from the seller in every transaction.

Please contact your underwriter if you have additional questions or concerns.

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¹ IRS Instructions for Form 8288 (Rev. 9-2015)