FOREIGN INVESTORS GUIDE

2022

PURCHASING REAL PROPERTY & DOING BUSINESS IN THE UNITED STATES

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Julian B. Myers is an attorney licensed to practice law in Mexico and California. Given his bi-cultural background, Mr. Myers is especially valuable in bridging the "cultural gap" that often arises in cross-border transactions. Julian B. Myers represents foreign and domestic clients with matters in the U.S. and abroad, assisting them with a wide variety of legal matters, such as:

CORPORATE AND BUSINESS

- Business planning and entity selection.
- Entity formation, ongoing maintenance and legal compliance.
- Operational matters and fundamental changes (i.e. registration in other jurisdictions, annual reports, conversions, mergers and acquisitions, etc.).
- Corporate finance and funding of business opportunities.
- Corporate and business tax.
- Planning, negotiating and documenting business transactions.
- Preparing proposals, letters of intent, memorandums of understanding and contracts.

REAL ESTATE

- Real estate transactions.
- Leasing.
- Real estate financing.
- Creation and disposition of rights to real property (easements, licenses, etc.).
- Planning and creation of real property ownership structures.

INTERNATIONAL TAX

U.S. Activities of Nonresident Aliens (Inbound):

- Planning and creation of corporate and business structures for nonresident aliens doing business or investing in the U.S.
- U.S. tax and pre-immigration planning for nonresident aliens.

- Real estate transactions and creation of ownership structures for nonresident aliens.
- Cross-border commerce and trade.
- Estate planning.

Foreign Activities of Permanent Residents and U.S. Citizens (Outbound):

- Planning and creation of corporate and business structures in foreign jurisdictions.
- Cross-border tax planning (creation of structures seeking to minimize tax and provide offshore asset protection).
- Real estate transactions and creation of real property ownership structures in foreign jurisdictions.

EDUCATION

- Diploma in Tax, University of San Diego School of Law (2013)
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SDAR FOREIGN REAL ESTATE INVESTORS GUIDE

INTRODUCTION

The purpose of this guide is to provide realtors a simple list of topics that they should consider and discuss when assisting "non-resident aliens" with their investments in U.S. real estate.

The information contained in this outline is intended to be of a general nature and based on laws that are subject to constant change. The applicability of the topics discussed herein to any particular situation should be carefully determined through consultation with an attorney or professional tax advisor.

1. FOREIGN INVESTOR STATUS.

1.1 Resident Alien and Nonresident Alien.

The applicability of U.S. tax laws varies depending on whether a person is "resident alien" or a "non-resident alien". Foreigners are typically recognized as "non-resident aliens" unless they obtain a permanent resident card (green card) or meet the "substantial presence test" (discussed in Section 1.2 below), in which case, they shall be considered "resident aliens" for tax purposes. It is also possible to be considered a non-resident alien for a part of the year and a resident alien for the rest of the year.

1.2 Green Card Test and Substantial Presence Test.

U.S. tax law states that a person will be considered a resident for tax purposes if he obtains a green card (becomes a permanent resident of the United States for immigration purposes) or meets the substantial presence test for the calendar year (becomes a resident due to the time spent in the United States).

Under the green card test the individual becomes a U.S. resident from the first day of actual physical presence in the U.S. after the “green card” is issued.

To meet the substantial presence test, a person must be physically present in the United States 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: (i) all the days the person was present in the current year, and (ii) 1/3 of the days the person was present in the first year before the current year, and (iii) 1/6 of the days present in the second year before the current year.

The presence of certain individuals is exempt from the "substantial presence" calculation, such as:

- An individual temporarily present in the United States as a foreign government-related individual under an “A” or “G” visa, other than individuals holding “A-3” or “G-5” class

visas.

- A teacher or trainee temporarily present in the United States under a "J" or "Q" visa, who substantially complies with the requirements of the visa.

- A student temporarily present in the United States under an "F," "J," "M," or "Q" visa, who substantially complies with the requirements of the visa.

- A professional athlete temporarily in the United States to compete in a charitable sports event.

1.3 Ending Tax Residency / Expatriation.

The tax residency of a person who meets the "substantial presence test" ends on the last day of such person's presence in the United States, followed by a period during which such person: (i) is not present in the United States; (ii) has a closer connection to a foreign country than to the United States; and (iii) is not a resident of the United States during the calendar year following that of the last day of presence in the United States.

The residency of a person that meets the "green card test" ends on the last day of presence in the United States on which such person is considered to be a lawful permanent resident of the United States; or, if such green-card holder resides outside the United States, until such person: (1) voluntarily turns in his green card to USCIS and renounces his U.S. immigrant status; (2) has his immigrant status administratively revoked by USCIS; or (3) has his immigrant status judicially revoked by a United States federal court.

A green card holder that gives up his green card (or a U.S. Citizen giving up his citizenship) may be subject to the "Expatriation Tax". This tax applies to U.S. Citizens or green card holders who have held a green card for at least 8 of the last 15 tax years and who meet one of the following conditions:

- The person's annual U.S. income tax liability during the last 5 years prior to the date of expatriation is greater than $171,000;

- The person's net worth is 2 million or more as of the date of expatriation; or

- The person fails to certify that he has complied with U.S. tax laws for the last 5 years prior to the date of expatriation.

If a person is deemed subject to the expatriation tax (a "covered expatriate") he shall pay income tax on the "fair market value" of all of his assets (as if such assets were sold on the day before expatriation) - subject to an exclusion amount of $737,000.

2. TAXATION OF NON-RESIDENT ALIENS.

If a person is considered a resident alien, he/she will be taxed in the United Sates in the same manner as a U.S. citizen is taxed. This means, that such person will be taxed on his/her worldwide income during the time he/she is a resident alien.

Non-resident aliens on the other hand, are only taxed in the United Sates on income derived from U.S. sources. This guide will focus primarily on "non-resident aliens".

There are two main types of income that a non-resident alien can receive from U.S. sources:

- U.S. Trade or Business Income; and
- Passive Income.

2.1 U.S. Trade or Business Income.

For non-resident aliens that are "engaged in a trade or business" in the United States, the net income that is "effectively connected" with such activities will be taxed in the same manner as it would if a U.S. citizen were involved. Of course, in order to generate trade or business income a non-resident alien must have a certain level of engagement in a specific activity in the United States. For example, the provision of services, either as an employee or an independent contractor with the United States, is considered to be "engaged in a trade or business" (to be distinguished from services performed outside the U.S., which would generate "foreign source income" not taxable in the United States). Likewise, a non-resident selling and distributing products in the United States through a partnership or a U.S. branch would also be considered to be "engaged in a trade or business" in the United States.

2.2 Passive Income.

Nonresident aliens are subject to a thirty percent (30%) flat tax on several types of passive income. This tax is applied on a gross basis, meaning that no deductions or exemptions are available to offset the tax and it is typically collected through withholding. The best examples of items of income that are subject to the 30% flat tax are interest, dividends, rents, royalties and "FDAP Income". FDAP Income means income that is "Fixed or Determinable Annual or Periodical". For example, a non-resident alien who owns and rents real property in the United States as an investment, will pay the 30% tax on the rent received from that business (unless an election is made to treat the income as being from a U.S. trade or business, in which case, the non-resident alien may claim deductions to offset the tax).

2.3 Disposition of U.S. Real Property Interests by Non-Resident Aliens.

Nonresident aliens are subject to U.S. tax on the gain from the sale or disposition of a U.S. real property interest, as if they were "engaged in a trade or business" in the United States. This means that such dispositions are taxed in the same way they would if a U.S. citizen were involved (giving rise to capital gains). The term "U.S. Real Property Interest" means an interest in real property (including an interest in a mine, well, or other natural deposit) located in the United States. It also means any interest, other than as a creditor, in any domestic corporation unless it is established that the corporation was at no time a "U.S. real property holding corporation" (USRPHC) during the shorter of the period during which the interest was held, or the 5-year period ending on the date of disposition. A U.S. corporation will be considered a USRPHC if the value of its real estate equals or exceeds 50% of the fair market value of its worldwide real property assets and any other assets used in its trade or business.

Under the "Foreign Investment in Real Property Tax Act of 1980", also known as "FIRPTA", the

disposition of a U.S. real property interest by a foreign person is subject to income tax withholding. The term "disposition" for FIRPTA purposes is very broad. It includes but is not limited to a sale or exchange, liquidation, redemption, gift, transfer, etc. The transferee of such real property interest must deduct and withhold a tax equal to 15% of the total amount realized by the foreign person on the disposition. The amount realized is the sum of (1) the cash paid, or to be paid (principal only), (2) the fair market value of other property transferred, or to be transferred, and (3) the amount of any liability assumed by the transferee or to which the property is subject immediately before and after the transfer. The amount realized is generally the amount paid for the property. If the property transferred was owned jointly by U.S. and foreign persons, the amount realized is allocated between the transferors based on the capital contribution of each transferor.

Withholding under FIRPTA is not required in the following situations (however, detailed notifications to the IRS are required):

1. The transferee acquires the property for use as a home and the amount realized (generally sales price) is not more than $300,000.

2. The property disposed of (other than certain dispositions of nonpublicly traded interests) is an interest in a domestic corporation if any class of stock of the corporation is regularly traded on an established securities market.

3. The disposition is of an interest in a domestic corporation and that corporation furnishes a certification stating, under penalties of perjury, that the interest is not a U.S. real property interest.

4. The transferor provides a certification stating, under penalties of perjury, that the transferor is not a foreign person.

5. The transferee receives a withholding certificate from the Internal Revenue Service that excuses withholding.

6. The transferor provides written notice that no recognition of gain or loss on the transfer is required because of a nonrecognition provision in the Internal Revenue Code or a provision in a U.S. tax treaty (this notice must be filed with the IRS by the 20th day after the date of transfer).

7. The amount the transferor realizes on the transfer of a U.S. real property interest is zero (i.e. a gift).

8. The property is acquired by the United States, a U.S. state or possession, a political subdivision thereof, or the District of Columbia.

9. The grantor realizes an amount on the grant or lapse of an option to acquire a U.S. real property interest. However, the transferee must withhold on the sale, exchange, or exercise of that option.

10. The disposition (other than certain dispositions of nonpublicly traded interests) is of publicly traded partnerships or trusts.

2.4 Gift and Estate Taxation.

The federal gift and estate taxes are a coordinated set of taxes that apply to gratuitous transfers of property. The gift tax is imposed on transfers made during a person's life. The estate tax imposes a tax on transfers made upon a person's death. The gift and estate taxes apply to all U.S. citizens and persons "domiciled" in the United States. The concept of "domicile" for gift and estate tax purposes differs from the definition of "residency" for immigration and income tax purposes. Courts have held that an individual's "domicile" is the permanent home to which the person ultimately intends to return (a subjective test). In 2022, U.S. citizens and persons "domiciled" in the United States have a $16,000 annual and a $12,060,000 lifetime unified exclusion from the gift and estate taxes.

The U.S. gift tax also applies to non-domiciled foreign nationals with respect to all transfers of real or tangible property situated in the United States (also known as U.S. Situs Property), but not intangible property, when the value of the gift exceeds the annual exclusion amount of $16,000. Gifts from a non-domiciled foreigner to a citizen spouse are generally not subject to the gift tax. However, gifts made by a citizen spouse to a non-domiciled foreigner spouse are capped at $164,000. Any gift in excess of these amounts is taxed at the highest rate of 40%

Likewise, the gross estate of a non-domiciled foreigner for purposes of the estate tax, shall be all property, tangible or intangible, situated in the United States (again, U.S. Situs Property), in which the deceased non-domiciled foreigner had an interest at the time of his death. For purposes of the estate tax, if the fair market value of the deceased non-domiciled foreigner's estate exceeds $60,000, the excess will be taxed at the highest rate of 40%

The gift and estate taxes present a particular problem for foreign nationals who take title to real property directly in their names and later wish to gift such property or happen to die without having a plan to address the resulting estate tax. This is a topic that will be further discussed throughout Section 3 below.

2.5 State and Local Taxes.

Many states collect income taxes on the income of residents and non-residents doing business in the state. Some states have no income tax. Some cities also impose income taxes in a like manner (often described as local taxes). Many of the state income taxes are based on federal income tax. Income tax rates vary widely from state to state, but are typically less than 10%. Examples of other state and local taxes include the sales tax, property tax, franchise tax, use tax and wealth tax. It is important to mention that many states have different ways of determining whether or not a person is a resident of that state (or a foreigner). Also, most states have no obligation to observe federal tax treaties.

In California, taxes are levied based on the filing status of the taxpayer. California has different filing statuses: i.e. single, married filing a separate return, married filing a joint return, surviving spouse, and head of household. There are nine tax brackets for each filing status, with marginal tax rates ranging from 1 percent to 12.3 percent, depending on a taxpayer’s income level. Also, an additional 1 percent tax (often called the 10^{th} bracket) is levied on the portion of taxpayers’ incomes in excess of $1 million, with the proceeds used for mental health services.

2.6 Filing and Reporting Requirements.

Resident aliens and non-resident aliens are both subject to filing a U.S. tax return if they derive income in the United States. Resident aliens typically file Form 1040 (U.S. Individual Tax Return) and non-resident aliens file Form 1040NR (U.S. Nonresident Alien Income Tax Return), on or before April 15 each year (although an extension can be requested).

Any person who files a U.S. tax return is required to provide a tax identification number. For resident aliens, this will typically be a "social security number" issued by the Social Security Administration. However, non-resident aliens are required to obtain an "Individual Taxpayer Identification Number" (ITIN), which is issued only for use regarding a non-resident alien's tax return.

2.7 Impact of U.S. Activities on Non-Resident Alien's Home Tax Laws.

When representing non-resident aliens, it is important to consider that even though a certain activity does not have a significant tax impact in the United Sates; it may have a substantial tax impact in the non-resident alien's home country. In other words, just because a disposition is tax free in the United States, it does not mean that it is will be tax free in that person's country of residence.

2.8 List of Countries with Tax Treaties with the U.S.

The United States has signed tax treaties with various countries. Under these treaties, residents of the foreign countries are taxed at a reduced rate, or are exempt from U.S. taxes on certain items of income they receive from sources within the United States. These reduced rates and exemptions vary among countries and specific items of income. Under these same treaties, residents or citizens of the United States are taxed at a reduced rate, or are exempt from foreign taxes, on certain items of income they receive from sources within foreign countries. Most income tax treaties contain savings clauses which prevent a citizen or resident of the United States from using the provisions of a tax treaty in order to avoid taxation of U.S. source income. If a treaty does not cover a particular type of income, or if there is no treaty between a non-resident's country and the United States, such non-resident must pay tax at regular rates.

The list of countries with tax treaties with the United States is subject to constant change, but currently, the U.S. has treaties with the following countries:

Armenia, Australia, Austria, Azerbaijan, Bangladesh, Barbados, Belarus, Belgium, Bulgaria, Canada, China, Cyprus, Czech Republic, Denmark, Egypt, Estonia, Finland, France, Georgia, Germany, Greece, Hungary, Iceland, India, Indonesia, Ireland, Israel, Italy, Jamaica, Japan, Kazakhstan, Korea, Kyrgyzstan, Latvia, Lithuania, Luxembourg, Malta, Mexico, Moldova, Morocco, Netherlands, New Zealand, Norway, Pakistan, Philippines, Poland, Portugal, Romania, Russia, Slovak Republic, Slovenia, South Africa, Spain, Sri Lanka, Sweden, Switzerland, Tajikistan, Thailand, Trinidad, Tunisia, Turkey, Turkmenistan, Ukraine, United Kingdom, Uzbekistan and Venezuela.

3. REAL ESTATE HOLDING STRUCTURES FOR NON-RESIDENT ALIENS.

3.1 Vesting Options Under California Law.

The California Land Title Association (CLTA) has provided a list of common vesting options as

an informational overview. As can be expected, the Association urges real property purchasers to carefully consider their titling decision prior to closing, and to seek counsel should they be unfamiliar with the most suitable ownership choice for their particular situation.

Sole Ownership

Sole ownership may be described as ownership by an individual or other entity capable of acquiring title. Examples of common vesting cases of sole ownership are:

- A "Single Man or Woman", an "Unmarried Man or Woman" or a "Widow or Widower" (i.e. a man or woman who is not legally married or in a domestic partnership);

- A "Married Man or Woman as His or Her Sole and Separate Property" (i.e. a married man or woman who wishes to acquire title in his or her name alone).

  In this case, the title company insuring title will require the spouse of the married man or woman acquiring title to specifically disclaim or relinquish his or her right, title and interest to the property. This establishes that both spouses want title to the property to be granted to one spouse as that spouse's sole and separate property. The same rules will apply for same sex married couples.

- A "Domestic Partner as His or Her Sole and Separate Property" (i.e. a domestic partner who wishes to acquire title in his or her name alone).

  In this case, the title company insuring title will require the domestic partner of the person acquiring title to specifically disclaim or relinquish his or her right, title and interest to the property. This establishes that both domestic partners want title to the property to be granted to one partner as that person's sole and separate property.

Co-Ownership

Title to property owned by two or more persons may be vested in the following forms:

- "Community Property": A form of vesting title to property owned together by married persons or by domestic partners. Community property is distinguished from separate property, which is property acquired before marriage or before a domestic partnership by separate gift or bequest, after legal separation, or which is agreed in writing to be owned by one spouse or domestic partner.

  In California, real property conveyed to a married person, or to a domestic partner is presumed to be community property, unless otherwise stated (i.e. property acquired as separate property by gift, bequest or agreement). Since all such property is owned equally, both parties must sign all agreements and documents transferring the property or using it as security for a loan. Each owner has the right to dispose of his/her one half of the community property by will.

- "Community Property with Right of Survivorship": A form of vesting title to property owned together by spouses or by domestic partners. This form of holding title shares many of the characteristics of community property but adds the benefit of the right of

survivorship similar to title held in joint tenancy. There may be tax benefits for holding title in this manner. On the death of an owner, the decedent's interest ends and the survivor owns all interests in the property.

- "Joint Tenancy": A form of vesting title to property owned by two or more persons, who may or may not be married or domestic partners, in equal interests, subject to the right of survivorship in the surviving joint tenant(s). Title must have been acquired at the same time, by the same conveyance, and the document must expressly declare the intention to create a joint tenancy estate. When a joint tenant dies, title to the property is automatically conveyed by operation of law to the surviving joint tenant(s). Therefore, joint tenancy property is not subject to disposition by will.

  Note: If a married person enters into a joint tenancy that does not include their spouse, the title company insuring title may require the spouse of the married man or woman acquiring title to specifically consent to the joint tenancy. The same rules will apply for same sex married couples and domestic partners.

- "Tenancy in Common": A form of vesting title to property owned by any two or more individuals in undivided fractional interests. These fractional interests may be unequal in quantity or duration and may arise at different times. Each tenant in common owns a share of the property is entitled to a comparable portion of the income from the property and must bear an equivalent share of expenses. Each co-tenant may sell, lease or will to his/her heir that share of the property belonging to him/her.

<u>Other Vesting Options</u>

- "Corporation": A corporation is a legal entity, created under state law, consisting of one or more shareholders but regarded under law as having an existence and personality separate from such shareholders. For tax purposes, a corporation also has existence and personality separate from such shareholders.

- "Partnership": A partnership is an association of two or more persons who can carry on business for profit as co-owners, as governed by the Uniform Partnership Act. A partnership may hold title to real property in the name of the partnership.

- "Trust": A Trust is an arrangement whereby legal title to property is transferred by a grantor to a person called a trustee, to be held and managed by that person for the benefit of the people specified in the trust agreement, called the beneficiaries. A trust is generally not an entity that can hold title in its own name. Instead title is often vested in the trustee of the trust.

- "Limited Liability Company": This form of ownership is a legal entity and is similar to both the corporation and the partnership. The operating agreement will determine how the LLC functions and is taxed. Like the corporation its existence is separate from its owners.

3.2 Problems that Non-Resident Aliens Face When Investing in U.S. Real Estate.

Having practiced law in the area of real estate for more than 10 years, representing mostly non-

resident aliens, the undersigned author has encountered many situations that are worth mentioning in this guide. However, the following are the most common (and damaging):

Taking Title Directly.

First and foremost, realtors need to bear in mind that the U.S. tax laws apply differently to non-resident aliens. For instance, while U.S. citizens and residents have an ample exclusion amount to work with regarding the estate tax ($12,060,000.00), non-resident aliens only have a $60,000 exclusion. To illustrate this problem, imagine that Juan Gomez, a Mexican citizen and non-resident alien, purchases a home outright in La Jolla for $5,000,000 and takes title directly in his own name. If Mr. Gomez dies, he will leave his family with an estate tax bill worth approximately $1.9 million. This is a huge tax burden and certainly not the result that Mr. Gomez had in mind when he first acquired the property. The same result if Mr. Gomez takes title to the property through a U.S. entity (i.e. corporation, LLC, partnership, etc.) because the ownership interest that Mr. Gomez holds at the time of his death is considered a "U.S. Situs Property" subject to the estate tax. The result is no different if Mr. Gomez places the property in a grantor trust – again, at the time of his death, his family will be dealing with property that is subject to U.S. estate tax. The same problem arises if in life Mr. Gomez "gifts" the property to his children or a non-resident spouse (as the real estate interest is U.S. Situs property, which will be subject to the gift tax).

Lack of Adequate Advice.

Second, realtors also need to understand that once a non-resident alien takes title to real property directly or under any of the vesting options typically utilized by U.S. citizens or resident aliens, it is difficult and expensive to transfer the property into a more beneficial structure (although it can be done with proper planning). This author has witnessed how some realtors rush their clients into closing and taking title to real property directly, under the assumption that title can be easily transferred into another holding structure at a later time. The undersigned has also witnessed how tax and legal professionals loosely advise their non-resident alien clients to transfer their real property (or real property interests) into more beneficial holding structures without complying with the numerous withholding and reporting requirements that the law imposes on non-resident aliens (i.e. filing tax returns and non-recognition transfer notices under FIRPTA). Overlooking these specific requirements is common because many advisors assume that the tax rules that apply to U.S. citizens or residents, also apply to non-residents. These mistakes and assumptions can make things a lot more difficult and expensive for non-resident clients down the road. For this reason, it is important to carefully plan and implement a non-resident's holding structure long before closing the real estate transaction.

3.3 Functional Holding Structures for Non-Resident Aliens.

As discussed in Section 3.2 above, some of the typical holding structures utilized by U.S. citizens or residents are inadequate for non-resident aliens. For instance, the typical "grantor trusts" that U.S. citizens and residents utilize to hold property (and avoid probate at the time of their death) do not shield a non-resident alien from the gift or estate tax. Likewise, putting real property into a U.S. corporation owned by a non-resident alien will not solve the problem either, because at the time of death, the non-resident alien will still own a U.S. Situs asset (i.e. the shares in the corporation). Of course, creating the perfect structure for a non-resident alien client is like making a suit to order. One must analyze the client's circumstances and goals and find the

best option that meets the client's specific needs. While one structure may work well for one client, it may be the worst option for another client.

"Joint Tenancy" and "Community Property" Vesting With "Right of Survivorship".

This type of vesting allows a non-resident alien to transfer real property to a spouse while avoiding probate and associated expenses at the time of his death. However, the estate tax will remain a problem (although the tax can be deferred to the time of death of the surviving spouse if a QDOT type trust is utilized). Unfortunately, the cost to create a QDOT trust can be substantial and the estate tax is only deferred, not avoided.

Grantor Trusts Coupled with Life Insurance Policy.

Grantor trusts are often used by non-resident aliens to hold real property, however, there generally is no income tax advantage in doing so (because the grantor is considered the owner of the trust's assets under the law). Thus, while a grantor trust will avoid probate at the time of a non-resident alien's death, it will not resolve the resulting estate tax problem. Nevertheless, grantor trusts can be effectively utilized as holding vehicles if a life insurance policy is purchased to pay the estate tax at the time of the grantor's death. In practice however, the cost to purchase a life insurance policy can easily exceed the cost involved with creating and maintaining any of the other holding options discussed below – which makes this a less attractive option.

Foreign Trusts.

Foreign trusts can be useful holding structures for non-resident aliens. In order to be effective, a foreign trust will typically need to be set-up as an irrevocable "foreign non-grantor trust". If structured correctly, there should be no estate tax at the death of the non-resident alien grantor (so long as he has not retained any powers). Creating and maintaining foreign trusts can be expensive and the applicable tax rules can be complex. A settlor under an irrevocable trust is also required to relinquish his/her ownership in the assets placed in the trust. This sometimes makes this option less desirable than the other holding options discussed below.

Foreign Entities

Investment in U.S. real estate through a foreign entity has many advantages. This option provides a non-resident alien with anonymity, limited liability and it helps to avoid the U.S. gift and estate tax. However, depending on the type of entity used, there are also disadvantages. For instance, "corporation" type entities can be exposed to the U.S. “branch profits tax” (unless the applicable rate is reduced under a tax treaty) and higher corporate income tax and capital gains rates. Also, foreign corporations are subject to FIRPTA withholding when they dispose of a U.S. real property interest and imputed rent for the personal use of the real property by its shareholders. "Partnership" type entities on the other hand (i.e. partnerships, LLCs, etc.) avoid most of the foregoing disadvantages applicable to corporations while at the same time providing its owners (called members) the benefit of a "one-level" (although typically higher) tax rate. However, FIRPTA applies to the disposition of a U.S. real property interest held by a foreign partnership as well as imputed rent for the personal use of the real property by its members.

Layered Offshore Holding Structures.

More often than not, the best type of holding structure that a non-resident alien can use to hold U.S. real property is a layered offshore holding structure. The way these structures work is that the non-resident alien forms an entity in a foreign jurisdiction which acts as a "blocker" (typically, his/her home jurisdiction) and this entity either acquires the property directly or forms an entity in the United States, which in turn acquires the real property. The main advantages of using a layered offshore holding structure are that, with careful planning, one can mitigate or avoid application of the U.S. estate tax, branch profits tax and double taxation. Depending on how the underlying U.S. entity is structured, a non-resident alien can also sell the property, pay a single level of tax and distribute the proceeds free of FIRPTA withholding.

3.4 Need for Proper Counsel.

When it comes to investing in U.S. real property, the U.S. tax regime requires special planning for non-resident aliens. The initial question is whether the individual is a non-resident alien. If the client is a non-resident alien, then realtors should bear in mind that they are dealing with a special case that requires detailed attention. When in doubt, the realtor and his/her non-resident client should seek competent legal advice in order to properly structure the proposed investment, taking into account the facts of each client's case.

4. CHECKLIST FOR REALTORS ASSISTING FOREIGN INVESTORS.

- Have you determined whether your client is a U.S. citizen or a resident alien (either because he/she is a "green card" holder or has he/she been physically present in the United States 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)?

- If your client is a "non-resident alien" do you have a full understanding of the proposed investment, the facts of the client's transaction, as well as his/her goals?

- Does your client understand his/her vesting options (or possible holding structures) and has he/she had an opportunity to discuss these options and their tax and legal ramifications with a professional advisor?

- If your non-resident client has in fact had an opportunity to discuss his/her vesting options (or possible holding structures) with a professional advisor, has he/she had an opportunity to create and implement the structure before closing the transaction?

While the foregoing questions are not designed to motivate a realtor to engage in the practice of law or provide legal or tax advice to a client, they are designed to raise awareness of the topics that should be considered before making an investment in U.S. real estate (or guiding a non-resident client to do so). If after considering these questions, a client has further questions or comments, he/she should retain the services of an attorney or a professional tax advisor.