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Not All Nonresident Aliens Required To Have Tax Withheld When Selling a Home; [FINAL Edition]

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Full Text (839 words)

QMy wife and I are nonresident aliens and we have owned our house in the United States for a number of years. We are going back home to Europe this summer and have put our house on the market. Because of the strong market, we expect to make at least $400,000 profit. We have lived in the home for at least four years and file a joint tax return. We were under the impression that we could take advantage of the "up to $500,000 exclusion" and not pay capital gains tax, but our real estate agent has advised us that the settlement attorney will have to withhold 10 percent of the sale price. Is that correct?

AProbably not.

The Foreign Investment and Real Property Tax Act (FIRPTA) sets the rules in your situation. The law dates to the 1970s, when Congress was concerned that foreigners had purchased U.S. real estate and, when they sold at a profit, took all of their money back home without paying taxes.

This complex law requires that in many situations, when a "foreign person" sells U.S. property, 10 percent of the net sales proceeds (called the amount realized) must be withheld and turned over to the Internal Revenue Service. According to the IRS, "withholding is intended to ensure U.S. taxation of gains realized on disposition of such interests."

When residential or commercial property is sold, the settlement attorney or title company is obligated to inquire whether the seller is a foreigner subject to the withholding requirements.

According to FIRPTA, a foreign person is a nonresident alien individual, foreign corporation that had not elected to be treated as a domestic corporation, foreign partnership or even foreign estate. It does not cover resident aliens.

If the seller (transferor) is covered by FIRPTA, 10 percent of the sale proceeds must be withheld at settlement, with some exceptions. If the money is not withheld, the IRS can look to the buyer for the tax.

The tax must be reported on IRS Form 8288 (or 8288-A) and must be transmitted to the IRS within 20 days after the property is transferred.

There are a number of exceptions to this withholding requirement. I think one of them covers you. They are:

If the buyer acquires the property for use as a principal residence and the sales price is less than $300,000, no withholding is required. According to the IRS, the buyer (or a member of the buyer's family) "must have definite plans to reside at the property for at least 50 percent of the number of days the property is used by any person during each of the first two 12- month periods following the date of transfer."

If the property is acquired by the United States, a state government or the District of Columbia.

If the seller does not realize any money on the sale of the property.

If the transferor gives the buyer (and the title attorney) written notice that no recognition of any gain or loss is required.

The last exception appears to apply in your situation. If you have owned and lived in your house here in the United States for at least two out of the five years before it is sold, and you and your wife will file a joint tax return, you are exempt from paying capital gains tax on up to $500,000 of the profit you will make on the sale of your house. (Single people and those not filing joint returns can exclude up to $250,000 each.)

U.S. citizens and resident aliens are not even required to report such a sale to the IRS. You, however, must be sure to give written notice to the title attorney that no recognition of gain or loss is required. You must make sure that your buyer -- or the title attorney -- files a copy of the notice with the IRS by the 20th day after the sale. You must also make sure that IRS Form 8288-B is filed. Although the law allows either the transferor or the transferee to file this form, it is recommended that you, as seller, take responsibility.

On closing day, the settlement lawyer will ask you to sign an affidavit of your citizenship. Make sure that you keep a copy of this affidavit as well as a copy of the written notice that you present to the lawyer at closing.

FIRPTA has serious complications for buyers, sellers, real estate agents and settlement companies. To be safe, consult your lawyer or financial adviser about your situation well before settlement.

For more information on FIRPTA, see IRS Publication 515, "Withholding of Tax on Nonresident Aliens and Foreign Entities." It's free at your local IRS office or on the Web (www.irs.gov).

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