
CORPORATE TAX PLANNING

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US REAL PROPERTY GAINS OF FOREIGN PERSONS: AN OVERVIEW FOR THE CANADIAN TAX PRACTITIONER

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Section 897, added to the Internal Revenue Code by the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA), is perhaps one of the most commonly overlooked taxes imposed by the United States. In a mergers and acquisitions context, it is generally an afterthought despite its broad application. Essentially, any transaction that involves a US real property interest can attract a FIRPTA liability, withholding tax, and/or a reporting requirement. Although not all transfers by foreign persons involving US real property interests will be taxable, virtually will require disclosure.

The stated purpose of FIRPTA is to equalize the US income taxation of gains from the sale of US real estate for both US and foreign investors. But what began as a response to perceived widespread US tax avoidance by foreign investors has become a tax regime of almost unmatched complexity.

FIRPTA can affect all forms of investment and types of investors—from the Canadian snowbird who buys a Florida condo to the corporation that owns a manufacturing plant in Detroit to the retail investor who purchases an interest in a US corporation or partnership. FIRPTA touches a wide range of transactions in the United States and, accordingly, should be considered when evaluating any form of US investment or divestiture.

The purpose of this article is to provide the Canadian tax practitioner with a basic understanding of the FIRPTA rules, which is fundamental to an analysis of the impact of this tax. The article examines (1) the US taxation of foreign persons in general and the taxation of real property gains before the enactment of FIRPTA; (2) the basic framework of FIRPTA; (3) the types of transactions to which FIRPTA can apply; and (4) FIRPTA's complementary withholding tax, which acts as a backstop to enforce collection of the FIRPTA liability.

KEYWORDS: FIRPTA ■ REAL PROPERTY ■ WITHHOLDING TAXES ■ US

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