



# Representing Foreign Buyers – Choice of Entity and Compliance: What You Don't Know May Hurt You

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# PATRIOT ACT – COMPLIANCE

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- The Patriot Act “blocks property and prohibits transactions with persons who commit, threaten to commit, or support terrorism.”
- SECTION 352(a) of the PATRIOT ACT requires financial institutions to establish anti-money laundering programs
- A financial institution as defined by the Act includes “persons involved in real estate closings and settlements”, however no additional regulations have been published to specifically require title companies or attorneys to establish comprehensive anti-money laundering programs required at other financial institutions (banks)

# PATRIOT ACT - COMPLIANCE

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- Financial Crimes Enforcement Network of the US Department of Treasury (FINCEN) has identified activities which pose greatest risk of money laundering:
  1. Payment of Funds for Real Estate from High Risk Country
  2. Sales Proceeds to be delivered to High Risk Country
  3. Title acquired in name of nominee without legitimate reason
  4. Person acting as agent for undisclosed principal
  5. Buyer not aware of their intended use of real estate
  6. Multiple acquisitions and sales within short time frame
  7. Request to misrepresent transaction in preparation of documents
  8. Suspicious identification

# PATRIOT ACT – COMPLIANCE

## PRACTICE POINTS

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- Office of Foreign Assets Control (OFAC) maintains a “Specially Designated Nationals and Blocked Persons List” (SDN) which the Fund incorporates into its name search database
  - If using ATIDS perform a 1-day name search on Buyer
  - Fund products includes this search as part of the product
- Notify financial institution (bank) where funds received if prospective buyer on SDN list is detected and cooperate with further requests from bank and government investigators (unless information protected by attorney client privilege) – seek Florida Bar guidance if unsure

# PATRIOT ACT – COMPLIANCE

## PRACTICE POINTS

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- Document explanation of use of nominees, powers of attorney, flip transactions and refuse to participate in transaction if a reasonable explanation cannot or will not be provided
- Avoid preparing settlement statements or documents that do not accurately reflect the substance of a transaction
- Obtain identification for all customers if not personally known

# FINCEN GEOGRAPHIC TARGETING ORDER

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- Current Order is from November 15, 2018
- Covers Palm Beach, Miami Dade and Broward Counties in Florida
- Order is no longer confidential
- Trusts are no longer within the scope of the current GTO



# FINCEN GEOGRAPHIC TARGETING ORDER

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- Criteria for Reporting – all criteria must be met to trigger the reporting obligation:
  - Residential only
  - Sales Price of \$300,000 or more
  - Involves transfer of funds (including virtual currency)
  - Institutional financing is not involved
  - Purchaser acquires title in a “Legal Entity” (defined in the GTO)
  - Within the targeted area – in Florida this currently covers Palm Beach, Miami-Dade and Broward

# FINCEN GEOGRAPHIC TARGETING ORDER

## Definitions

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- Legal Entity – corporation, limited liability company, partnership or other similar business entity, whether formed under the laws of a state, or of the United States, or a foreign jurisdiction
  - previous version of GTO included trusts and these are no longer covered
- Residential - From 31 CFR Chapter X Section 1010.100 -
  - (A) A residential structure that contains one to four units, including, if used as a residence, an individual condominium unit, cooperative unit, mobile home or trailer; or
  - (B) Residential real estate upon which such a structure is constructed or intended to be constructed



# FINCEN GEOGRAPHIC TARGETING ORDER

## Reporting

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- Report due within 30 days of transaction (closing)
- Use FINCEN Currency Transaction Report
- Must obtain photo identification, contact information and occupation for person responsible (President/Manager) and all beneficial owners with more than a 25% interest
- Also requires reporting details of transaction and source of funds
- May use the Fund or file directly – Fund is now encouraging direct filing
- Criminal and civil penalties for failure to comply

# Florida Alien Business Organization Registration

## Florida Statute 607.0505

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- Alien Business Organization - foreign corporation or other entity organized under the laws of a jurisdiction outside of the United States
- Must designate a Registered Agent in Florida if the entity owns real estate
- Alien Business Organizations which also rent property in Florida must file under the Registration to do Business Statutes (similar to domestic entities)
- Registered Agent must have information about owners and be able to produce this information within 30 days
- Statute provides that privilege is waived as part of the registration with respect to the matters covered (e.g. identity of owners)
- Does not apply to domestic entities

# Foreign Investment in Real Property Tax Act (FIRPTA)

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- All foreign individuals and corporations disposing of a US real property interest must pay income tax on the sale of the US real property interest (USRPI) regardless of any treaty provisions – 26 USC 897
- US real property interest defined as (i) real estate (including mineral rights) within the United States or Virgin Islands and (ii) stock in a US Real Property Holding Corporation (USRPHC)
- A USRPHC is a corporation whose assets primarily (over 50%) consist of US real estate compared to all of its real estate (worldwide) and other assets used in a trade or business

# Federal Income Tax on Sale of Real Estate (Capital Gain)

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- Short term capital gain vs. Long Term capital gain
  - 1 year or less is short term capital gain
  - Short term capital gain taxed at individual income tax rates
  - Long term capital gain generally taxed at 20%
- Corporate Income tax for C Corporation – 21% - change from former progressive schedule as a result of 2017 Tax Cuts and Jobs Act of 2017

# Corporation, Partnership or Disregarded – Entity

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- C Corporation – Foreign corporation, US corporation that does not make Subchapter S election and others electing this tax treatment
  - Subchapter S election only available if all owners US persons
- Pass through entities (e.g. partnerships) – file an informational return identifying the owners and their respective % of income/expenses and the owners then file tax returns to report and pay tax
- “Check the Box” – choice of how an entity is taxed is very flexible and an LLC can elect to be taxed as C corporation or as a pass-through entity (even if there is only one member)
- Disregarded Entity – not treated as a separate taxable entity and does not need to file a return – all income reported by the owner
  - Examples – typical single member LLC, living trust

# FIRPTA Withholding

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Transferee (buyer) must withhold 15% of gross sales price in a purchase of real estate from a seller with exceptions:

- Seller is a US person and provides Non FIRPTA Affidavit with tax identification number (social security number or employer identification number)
- Sale is less than \$300,000 and (i) buyer takes title as individual(s), and (ii) buyer intends to use property primarily for personal use for each of the first two years of ownership (not rental)

# FIRPTA Withholding Additional Exceptions

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Transferee (buyer) must withhold 15% of gross sales price in a purchase of real estate from a seller with exceptions:

- Withholding can be reduced to 10% for sales that are \$300,000 or more and less than \$1M where (i) buyer takes title as individual(s), and (ii) buyer intends to use property primarily for personal use for each of the first two years of ownership (not rental)
- Seller obtains Reduced Withholding Certificate from IRS in response to application filed on or before the closing date

# FIRPTA Withholding

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- When withholding is mandatory the following must be complied with:
  1. Unless a reduced withholding application has been applied for on or before the closing date funds must be sent to IRS within 20 days of closing or substantial penalties and interest apply
  2. If a reduced withholding application has been filed on or before the closing date, but IRS has not yet approved then funds are held in escrow with a Withholding Agent (Closing Agent or Seller's attorney) until IRS approval is obtained
  3. Seller and Buyer must each have a Social Security Number, US International tax identification number (ITIN) or Employee Identification Number (EIN) or apply for one



# US Estate Tax

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- US Estate tax applies to US real estate and tangible personal property
- Estate tax rates are very high and apply to entire value of property (not just the profit) – rates quickly progress over 30% and are capped at 40%
- Foreign persons from nations that do not have estate tax treaties with the US have a very small exemption (\$60,000 exemption equivalent to \$13,000 credit) unlike that of a US domiciliary (current exemption \$11.4M in 2019)
- Canada, UK, Italy, Germany have estate tax treaties with the US and the IRS maintains a complete list on their website along with text of the treaties – no South American country presently has an Estate tax treaty with the US



*Thank You!*  
for attending