ESCROW DOCUMENTS EXPLAINED

THE CAL-FIRPTA WITHHOLDING

Unless you have a reason to be familiar with tax laws, you are probably wondering, "what is FIRPTA?".

FIRPTA stands for Foreign Investment in Real Property Tax Act. It is a tax law that ensures foreign taxpayers pay income tax on their sale of US real estate.

WHY WAS FIRPTA CREATED?

For U.S. Citizens, capital gains tax money is taken out of your regular income tax. In contrast, foreign persons are taxed only on certain items of income and are not taxed on most capital gains items, including real estate. This being the case, FIRPTA was put into place to ensure that the government gets their piece of the pie when a foreign person living in the US sells real estate. It applies to almost any sale where a foreign owner of a US property sells said property.

FEDERAL WITHHOLDINGS:

To ensure the taxes are collected, buyers of real estate that falls under this tax act are required to withhold 10% of the sales price from the seller and deposit it with the IRS. This 10% deposit is applied to taxes owed on the sale (or transfer) of the property. If the actual taxes are calculated to be less than 10% of the sales price, the seller will receive a refund for the difference. If no taxes were owed, the entire deposit is refunded to the seller.

STATE WITHHOLDINGS:

Separate from the federal withholding requirements of FIRPTA, some states require buyers to withhold an additional amount to cover taxes that may be owed by sellers, even if the sellers are US citizens who reside in that state. For example, California requires that 3 1/3% of the sales price be withheld by buyers and deposited with the state's Franchise Tax Board, whether the seller is or is not a Californian resident. Just like the federal deposits, the seller receives a refund if taxes owed turn out to be less than the amount withheld.

EXEMPTIONS TO THE RULE:

If one or more of these circumstances apply, a seller may be exempt from this law:

The sales price is less than $100,000 and the buyer has definite plans to reside in the home for at least 50% of the first 24 months that the property is being used by any person

The seller provides written certification that they are not a foreign person

The buyer receives a withholding certificate from the IRS that excuses the withholding

The amount the seller realizes on the sale or transfer of the property interest is zero

Please Note: Inter Valley Escrow does not provide legal or tax advice.
Please consult your attorney or tax consultant before completing these forms.