What foreign investors need to know when investing in New York properties - by Joseph Aquino

August 23, 2022 - Front Section

Every now and then one gets a day that holds a delightful surprise and mine was the day I met Vince Rocco who taught at the New York Real Estate Institute near Macys Flagship store on 36th St. Yes, I could have done the course on-line, but why waste an opportunity to meet fellow real estate brokers. Isn't that what it's all about, brokers must continually network to make contacts to get business…

Vince is an amazing broker who is the senior member and longest tenured director of sales in the department which specializes in new condo development for Brown Harris Stevens. He also has his own talk radio / podcast called; Good Morning New York Real Estate, that has an audience of 45,000 listeners. Vince came out of the corporate world and now has 20 years of experience in the real estate industry.

Here are some stats and tips and Vince gave for foreign investors and for brokers to know when guiding your foreign investor into a transaction.

The top U.S. destinations for foreign buyers (July 2022) were: Florida, California, Texas, Arizona, New York, and North Carolina.

The top five countries undertaking foreign investment in the US today according to NAR are: China, Canada, UK, Mexico, and India.

Foreign Taxes

Establishing a proper tax and ownership structure for owning New York real estate is one of the most important first steps for any foreign investor. Yet, it's one that such investors often overlook; the federal government, New York State, and New York City each impose an income tax on rental income generated by properties within New York City. The combined rates of these taxes can be as high as 65% (including tax on repatriation of profits). These taxes also apply to gains from the sale of property.

In addition, both the federal government and New York state impose estate taxes on the value of property transferred at a person's death.

For foreign owners of U.S. property, the federal government imposes up to a 40% tax, and the New York government imposes up to a 16% tax, on the value of an estate to the extent that it exceeds $60,000. However, foreign buyers can minimize their income and estate-tax liabilities by structuring their U.S. holdings through a domestic or foreign trust or business entity, such as a corporation, limited liability company, or a foreign counterpart to those entities. Doing so requires proper advance planning with the assistance of a knowledgeable attorney.

Selling the Property: Taxes

The holding structure also affects the taxes due on sale of the property. An improper structure can result in taxes of up to 65% on income from the sale, including taxes on repatriation of the proceeds to the owner's home country.

In addition, foreign owners of New York real property must be aware of the Foreign Investment in Real Property Tax Act (FIRPTA) and similar New York withholding requirements.

FIRPTA requires a person who buys U.S. real property from a foreign seller to withhold 15% (if the purchase price exceeds $1 million) of the gross purchase price—not profits—and remit the withheld amount to the IRS. New York similarly requires withholding 8.82% of the projected capital gain realized from the sale. These withholding requirements can result in the seller not having enough funds to cover his or her closing expenses.

However, with proper planning, FIRPTA withholding can be reduced or eliminated. For more on this subject, see How Foreign Investors Can Reduce or Eliminate FIRPTA Withholding Upon Sale of U.S. Real Estate.

When selling a property in New York City, what taxes does a foreigner need to pay? A foreign person needs to pay gains tax and FIRTPA withholding tax. Federal capital gains tax is currently 20% of the net capital gain. Net capital gain is the amount of the gain on the property minus the original purchase price, closing costs, and capital improvements (renovations).

Similarly, New York State charges an 8.82% non-resident gains tax on the net capital gain. A foreign seller is responsible for submitting a withholding named FIRPTA.

FIRPTA imposes taxes on nonresident aliens and foreign corporations when they have Effectively Connected Income (ECI). This sounds complex, and it can be.

ECI is income that an individual or entity makes when engaged in a trade or business within the U.S. The gain from selling a U.S. property qualifies as such income.

And there is more to it, beyond just a sale of real property. The IRS taxes foreigners on the "disposition of U.S. real property interests." What does that mean?

Simply put, the IRS taxes any sale or transfer of foreign-owned real estate and other related ownership. The tax applies not only to individuals who are non-U.S. citizens or residents but also to foreign companies.

You are advised to seek out professional counseling.

Joseph Aquino is president of JAACRES, New York, N.Y.