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REAL ESTATE

Basic U.S. and Canadian Tax Considerations of Canadian Investment in U.S. Real Estate

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This article attempts to summarize the unique cross-border tax consequences surrounding a Canadian's acquisition of U.S. real property interests.

Canadians actively invest in U.S. real estate by speculating on land and developing homes, condominiums, shopping centers, and commercial buildings. Canadian investors generally have the same goals of minimizing their income tax liabilities from their U.S. real estate investment as do their U.S. counterparts. However, their objectives are complicated by the very fact that they are not U.S. persons. That is, Canadian investors must be concerned not only with income taxes in the United States, but also Canadian taxes. Further, the United States has special income tax regimes that are applicable to foreign persons. This article attempts to summarize the unique cross-border tax consequences surrounding a Canadian's acquisition of U.S. real property interests. This article will discuss the tax considerations associated with different ways a Canadian investor may hold U.S. real property.

U.S. INCOME TAX CONSEQUENCES OF DIRECTLY HOLDING U.S. REAL ESTATE

The simplest way for a Canadian investor to acquire U.S. real estate is to purchase it outright. Although holding U.S. real property outright is easy to understand, there are a number of complications associated with holding rental property outright. If a Canadian investor owns real property that is income producing, he or she will likely be required to file tax returns in Canada and the United States reporting the U.S. rental income. The income tax consequences of the U.S. rental income would be determined under both Canadian and U.S. tax laws, and the Canadian investor would likely be subject to both U.S. and Canadian income tax. There are also differences in compliance rules to consider. For example, the U.S. rules relating to depreciation, interest deductions, and foreign exchange gains differ from the Canadian rules.

A Canadian investor in income producing real property must understand U.S. source income received by foreign persons are subject to two basic taxing regimes. Most forms of U.S.-source income received by foreign investors that are not effectively connected with a U.S. trade or business will be subject to a flat tax of 30 percent on the gross amount of income received.

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Sections 871(a) (for nonresident aliens) and 881(a) for foreign corporations impose the 30 percent tax on "interest, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other enumerations is sometimes referred to as "FDAP income." The collection of such taxes is affected primarily through the imposition of an obligation on the person or entity making the payment to the foreign person to withhold the tax and pay it to the Internal Revenue Service or ("IRS"). If a foreign investor is engaged in a trade or business in the United States, the effectively connected income will be taxed and subject to U.S. graduated income tax rates.

If a Canadian investor receives rental income from U.S. real estate, it must be determined if the ownership of the U.S. real property can be classified as a U.S. trade or business. If the rental of U.S. real estate can be classified as a U.S. trade or business, the rental income will be taxed at graduated rates for U.S. tax purposes. Deductions may also be claimed to reduce the U.S. tax liability associated with the rental activity.

Even if the holding of U.S. real estate cannot be classified as a trade or business, Internal Revenue Code Sections 871(d) and 882(d) permit a foreign corporation or foreign investor that receives rental income from U.S. real estate to elect to be taxed on a net basis at graduated rates for U.S. federal income tax purposes. If a Canadian investor receives rental income from U.S. real estate and the activity cannot be treated as a U.S. trade or business or an election is not made to tax the rental income on a net basis, the gross rental income received by the Canadian investor will be subject to a 30 percent withholding tax. This withholding rate is not reduced under the United States-Canada Income Tax Treaty. (See exception below for contingent interest.)

FIRPTA CONSIDERATIONS

Any Canadian investor considering acquiring U.S. real estate must understand the Foreign Investment in Real Property Tax Act of 1980 ("FIRPTA"). Under FIRPTA, gains or losses realized by foreign corporations or nonresident alien individuals from any sale, exchange, or other dispositions of a U.S. real property interest are taxed in the same manner as income effectively connected with the conduct of a U.S. trade or business. This means that gains from dispositions of U.S. real property interests are taxed at the regular graduated rates, whereas losses are deductible from effectively connected income.

For this purpose, an "interest" in real property means any interest (other than an interest solely as a creditor), including fee ownership, co-ownership, a leasehold, an option to purchase or lease property, a time-sharing interest, a life estate, remainder, or reversion interest, and any other direct or indirect right to share in the appreciation in value or proceeds from the sale of real property.

A U.S. property interest also includes interest (other than an interest solely as a creditor) in a domestic corporation that was a U.S. real property holding corporation at any time during the five-year period ending on the date of the disposition of such interest or, if shorter, the period the nonresident held the interest. This prevents foreign persons from avoiding the FIRPTA tax by incorporating their U.S. real estate investment and then realizing the resulting gains through stock sales which may be exempt from U.S. tax.

To ensure collection of the FIRPTA tax, any transferee or buyer acquiring a U.S. property interest must deduct and withhold a tax equal to 15 percent of the amount realized on the disposition. A transferee is any person, foreign or domestic, that acquires a U.S. real property interest by purchase, exchange, gift, or any other type of transfer. The amount realized is the sum of the cash paid or to be paid, the market value of other property transferred or to be transferred, the amount of liabilities assumed by the transferred, and the amount of liabilities to which the transferred property was subject. Withholding requirements also apply to distributions made by a domestic or foreign corporation, partnership, estate, or trust, to the extent the distribution involves a U.S. real property interest, as well as to dispositions of interests in a partnership, trust, or estate that has a U.S. real property interest.

If the buyer is an individual person who will acquire the real property for personal use as a "personal residence," there is an exception to the FIRPTA withholding rules. If the sales price is $300,000 or less, then the tax withholding is not required. To qualify under the personal residence exemption, the transferee or certain members of the transferee's family (including brothers, sisters, spouses, or lineal descendants) must intend to reside at the property for more than 50 percent of the number of days that the property is used by any person for residential purposes during each of the two years following the acquisition of the property.

If the sales price of U.S. real estate is equal to or greater than $300,001, but equal to or less than $1 million then the seller would qualify for reduced withholding in the amount of 10 percent (instead of 15 percent). If the sales price is greater than $1 million, then no exception applies, and the buyer is responsible for withholding 15 percent of the amount realized by the seller.

EFFECTS OF INTERNAL REVENUE CODE SECTION 897

A Canadian investor may consider utilizing a shared appreciation mortgage to mitigate the impacts of FIRPTA. Internal Revenue Code Section 897 details the rules governing FIRPTA. Section 897 was designed to counteract the use of various techniques that had been developed to avoid income tax on the disposition of U.S. real estate. Section 897 imposes a tax on gain realized upon the disposition of a "U.S. real property interest." However for purposes of Section 897, a U.S. real property interest does not include an "interest solely as a creditor *** in real property."[1] Thus, a loan in which the lender has a direct or indirect right to share in the increase in value or the proceeds of the disposition of property will not be regarded as an interest solely as a creditor.[2]

Treasury Regulation Section 1.897-1(d)(2)(i) elaborates on the phrase "an interest other than an interest solely as a creditor" by stating it includes "any direct or indirect right to share in the appreciation in the value, or in the gross or net proceeds or profits generated by, the real property."

The Income Tax Regulation goes on to state that a "loan to an individual or entity under the terms of which a holder of the indebtedness has any direct or indirect right to share in the appreciation in value of, or the gross or net proceeds or profits generated by, an interest in real property of the debtor or of a related person is, in its entirety, an interest in real property other than solely as a creditor." Accordingly, a shared appreciation mortgage that is tied to U.S. real estate is a United States real property interest ("USRPI") for purposes of Internal Revenue Code Section 897.

Holding a USRPI will not trigger a U.S. tax obligation. However, when the foreign investor liquidates the USRPI, the foreign investor will be subject to U.S. tax under Section 897 to the extent that the USRPI is disposed of." Treasury Regulation Section 1.897-1(g) provides that disposition "means any transfer that would constitute a disposition by the transferor for any purpose of the Internal Revenue Code and regulations thereunder." In regards to shared mortgage sharing agreements, Treasury Regulation 1.897-1(h), Example 2, outlines a tax planning opportunity for foreign investors investing in U.S. real estate. In Example 2, a foreign corporation lends $1 million to a domestic individual, secured by a mortgage on residential real property purchased with the loan proceeds. Under the loan agreement, the foreign corporate lender will receive fixed monthly payments from the domestic borrower, constituting repayment of principal plus interest at a fixed rate, and a percentage of the appreciation in the value of the real property at the time the loan is retired.

The example states that, because of the foreign lender's right to share in the appreciation in the value of the real property, the debt obligation gives the foreign lender an interest in the real property "other than solely as a creditor." Nevertheless, the example concludes that Internal Revenue Code Section 897 will not apply to the foreign lender on the receipt of either the monthly or the final payments, because these payments are considered to consist solely of principal and interest for U.S. federal income tax purposes. Example 2 concludes that the receipt of the final appreciation payment that is tied to the gain from the sale of the U.S. real property does not result in a disposition of a USRPI for purposes of Section 897, because the amount is considered to be interest rather than gain under Internal Revenue Code Section 1001. The example does note, however, that a sale of the debt obligation by the foreign corporate lender will result in gain that is taxable under Internal Revenue Code Section 897.[3]

Consequently, Canadian investors may use debt instruments with contingent interest features to mitigate their exposure to FIRPTA. This does not mean that using a shared appreciation mortgage avoids U.S. tax on the sale of U.S. real property. Instead, a shared appreciation mortgage requires the lender to treat the receipt of contingent deferred interest as interest rather than capital gain. For example, in *Dorzback v. Collison*, 195 F.2d 69 (3rd Cir. 1952), a debtor/creditor relationship was amended to provide that, in lieu of interest at the rate of 5 percent per annum, the creditor would receive 25 percent of the net profits of the debtor's business. The court quoted the United States Supreme Court in defining interest as being "the amount which one has contracted to pay for the use of borrowed money." The court also noted that payments made in lieu of interest were in fact to be treated as interest, and that it was not a requirement that the interest be computed at a stated or fixed rate, but only that it be an ascertainable amount. In *Kena, Inc. v. Commissioner*, 44 B.T.A. 217, 219-20 (1941), the borrower and lender entered into an agreement in which the borrower received a sum of money as a "loan;" the borrower agreed to repay the principal and to pay a further sum "in lieu of interest" equal to 80 percent of the net profits of the borrower's business. The court held that the agreement was one creating a relationship of creditor and debtor, and that the amount paid for the use of the borrowed money was interest.

In order for the contingent interest of a shared appreciation mortgage to be recognized by the IRS, at a minimum, the debt instrument must contain the following terms: 1) the terms of the loan should contain a definite maturity date as well as a cap on interest participation; 2) the loan should not be convertible into an equity interest for the borrower; 3) the lender should not have effective control over the borrower or the borrower's assets exceeding that which a lender ordinarily would have; 4) there should be sufficient security for the debt; 5) the loan should be recourse in nature, rather than nonrecourse; 6) there should not be a provision in the loan under which the purported lender is obligated to subordinate to some or all the borrower's gross receipts rather than on its net income.

Although interest received by a Canadian real estate investor will not likely be subject to Section 897 and the FIRPTA withholding provisions of the Internal Revenue Code, any taxable gain will be treated as interest under the FDAP rules. This means contingent interest that may be received by a Canadian investor through a shared appreciation mortgage is subject to the 30 percent FDAP withholding provisions discussed above. Although contingent interest is FDAP and typically subject to a 30 percent withholding tax, the withholding tax on contingent interest may be eliminated or reduced for Canadian investors under Article XI of the U.S.-Canadian income tax treaty.

U.S. ESTATE AND GIFT TAX CONSIDERATIONS

Canadian investors often transfer U.S. real estate by devise or by gift. A transfer of U.S. real property by gift or at death may trigger the U.S. estate or gift tax. The United States imposes estate and gift taxes on certain transfers of U.S. situs property by "nonresident citizens of the United States." The U.S. estate and gift tax is assessed at a rate of 18 to 40 percent of the value of an estate or donative transfer. A foreign investor's U.S. taxable estate or donative transfer is subject to the same estate tax rates and gift tax rates applicable to U.S. citizens or residents, but with a substantially lower unified credit. The current unified credit for individual foreign investors or nonresident aliens is equivalent to a $60,000 exemption, unless an applicable treaty allows a greater credit. U.S. citizens and resident individuals are provided with a far more generous unified credit from the estate and gift tax. U.S. citizens and resident individuals are permitted a unified credit of $13,610,000 or $27,220,000 for a married couple (for the 2024 calendar year).

Article XXIX(B) of the U.S.-Canada income tax treaty provides relief from the U.S. estate tax for Canadian investors in U.S. real estate. Under the treaty, a Canadian real estate investor is entitled to relief from the U.S. estate tax, but the treaty does not provide any relief from the U.S. gift tax. Under the U.S.-Canada income tax treaty, a Canadian investor can claim a pro rata portion of the U.S. unified credit for estate tax purposes. The pro rata portion is based on the percentage of the individual's gross U.S. estate and gross worldwide estate. For example, assume a Canadian investor owns a vacation home in Florida with a value of $5 million that is unencumbered by a mortgage at his death in 2024. Let's also assume the Canadian investor's worldwide assets were valued at $5 million. Because the value of the Canadian investor's global assets did not exceed $13,610,000 on the date of his death, the estate of the Canadian investor will not be subject to U.S. estate tax.

HOLDING U.S. REAL PROPERTY THROUGH A NONGRANTOR TRUST

Instead of holding U.S. real property directly, a Canadian real estate investor may elect to hold U.S. real estate through a nongrantor trust. For U.S. income tax purposes, a nongrantor trust is taxed largely in the same manner as a U.S. person. However, for U.S. purposes, a nongrantor trust is taxed at compressed rates. Many Canadian investors utilize nongrantor trusts as a vehicle to avoid U.S. estate and gift taxes. Nongrantor trusts can also be utilized to avoid the U.S. branch profits tax (discussed below).

OWNERSHIP OF U.S. REAL PROPERTY BY A CANADIAN COMPANY OR CORPORATION

A Canadian investor may hold U.S. real estate through a Canadian company or corporation. For Canadian purposes, corporations are usually owned by multiple people, while companies can be owned by one individual. If a Canadian investor holds U.S. real property through a Canadian company or corporation, it would be required to file income tax returns in Canada and the United States. Income taxes paid to the U.S. could potentially qualify for a foreign tax credit under Canadian tax law and be utilized to reduce Canadian income tax liability. If a Canadian company carries on a U.S. trade or business such as renting U.S. real property, the Canadian company or Canadian corporation will be required to file U.S tax returns. A Canadian corporation and Canadian company is considered a per se corporation for U.S. tax purposes. This means that a Canadian real estate investor that holds U.S. real estate through a Canadian company or Canadian corporation must report any U.S. taxable gains on a U.S. corporate tax return and pay U.S. corporate tax.

Holding U.S. real property in a Canadian holding company can trigger the U.S. branch profits tax. Section 884(a) imposes a branch profits tax on effectively connected income of a U.S. branch of a foreign corporation when those earnings are repatriated, or deemed repatriated, to the home office of the branch. The branch profits tax equates to a tax equal to 30 percent of the corporation's dividend equivalent amount for the taxable year, subject to treaty reductions. Internal Revenue Code Section 884 describes the tax base for the branch profits as the "dividend equivalent amount," which is defined as the "effectively connected earnings and profits" with certain adjustments. It is intended to be the functional equivalent of earnings distributed as dividends by a subsidiary either out of current earnings not invested in subsidiary assets or out of accumulated earnings withdrawn from such investment. The amount taxed is reduced, therefore, by any increase in the branch equity. Conversely, the amount of earnings taxed is increased by a reduction of branch equity but not in excess of effectively connected earnings and profits accumulated at the end of the prior tax year. Branch equity is measured by the adjusted basis of branch assets less liabilities connected with the branch. Article X of the U.S.-Canada income tax treaty reduces the branch profits tax to a rate of 5 percent on net income exceeding 500,000 Canadian dollars.

Canadian investors often obtain financing from outside the United States to acquire U.S. real estate. Although interest paid to a foreign lender is typically deductible for U.S. and Canadian income tax purposes,[4] the U.S. rules governing the deduction of interest paid to a foreign lender is limited by Section 163(j) of the Internal Revenue Code. The general rule of Internal Revenue Code Section 163(j) limits the deductibility of interest expenses paid or accrued on debt properly allocable to a trade or business to the sum of business interest income, and 30 percent of "adjusted taxable income." Adjusted taxable income is determined without regard to certain deductions, including those for net interest expense, net operating loss carryforwards, depreciation, amortization, and deletion ("EBIT"). Any deduction in excess of the limitation is carried forward and may be used in a subsequent year, subject always to the limitations of Internal Revenue Code Section 163(j) (i.e., business interest income plus 30 percent of EBIT).

Canadian investors utilizing financing to acquire U.S. investment property should understand that the differences in how Canada and the United States treat deductible interest income may result in the amount of interest that is deductible in the United States being different from the amount deductible in Canada.

Upon the sale or exchange of U.S. investment property, a Canadian corporation and a Canadian company will be subject to U.S. and Canadian tax on gains realized on the sale of the U.S. real estate. Canadian corporations and Canadian companies holding U.S. real estate will also be subject to FIRPTA withholding tax. However, in certain situations a Canadian corporation or Canadian company may avoid FIRPTA withholding tax by making a Section 897(i) election with the IRS.[5]

USING A U.S. CORPORATION TO HOLD U.S. INVESTMENT REAL PROPERTY

A Canadian company or corporation may form a wholly owned U.S. corporate subsidiary to acquire U.S. real estate. Such a structure may be subject to Canada's Foreign Accrual Property Income or ("FAPI") for Canadian tax purposes. The FAPI regime is intended to prevent Canadian residents from avoiding Canadian income tax on passive investment income earned through a controlled foreign affiliate. The FAPI rules only apply to passive income held in a corporation.

If the U.S. company earns active business income, its Canadian parent would not be taxed in Canada on the dividends it receives from the U.S. company from active business earnings. Article X of the U.S.-Canada income tax treaty may reduce the U.S. tax on dividends to 5 percent of the gross amount of the dividend if the beneficial owner is a company which owns at least 10 percent of the voting stock of the company paying the dividends. However, the 5 percent U.S. tax on dividends would not likely qualify for a foreign tax credit in Canada. With that said, if the U.S. company holding U.S. real estate is liquidated after the real property is sold and U.S. corporate taxes have been paid, it is possible to have U.S. withholding taxes on dividends.

The U.S. branch profits tax rules will apply to structures in which a Canadian company forms a U.S. corporation to hold U.S. real estate. The operation of the branch profits tax can be demonstrated in a simple example. Cranberry, a Canadian company, has net equity (adjusted basis of U.S. corporate assets less U.S. corporate liabilities) in its wholly owned U.S. corporation at the end of tax year 1 of $4,500,000. Cranberry has effectively connected earnings and profits (effectively connected net income less U.S. income taxes) for tax year 2 of $1,000,000. The company acquired an additional $500,000 of U.S. assets during tax year 2 bringing its U.S. net equity at the end of tax year 2 to $5,000,000. Cranberry's dividend equivalent amount is equal to its effectively connected earnings and profits reduced by the amount of its increase in U.S. net equity ($1,000,000 - $500,000). Its dividend equivalent amount for year 2 is, therefore, $500,000. A branch profits tax of $150,000 (30% X $500,000 = $150,000) would typically have to be paid in addition to the U.S. tax on tax year 2 taxable income of the U.S. corporation. However, the U.S.-Canada tax treaty reduces the branch profits tax to a rate of 5 percent on net income exceeding 500,000 Canadian dollars. Since Cranberry is a resident of Canada, any branch profits would be reduced to 5 percent of the dividend equivalent after applying the 500,000 Canadian dollar exclusion.

Although foreign investors often utilize a U.S. corporation as a vehicle to hold U.S. real property, this type of planning option is risky. Canadian investors considering forming a wholly owned U.S. corporate subsidiary to acquire U.S. real estate should understand that the U.S. corporation will be considered a U.S. person for purposes of the Controlled Foreign Corporation or ("CFC") rules.[6] For purposes of the CFC rules, certain attribution rules can apply to attribute stock ownership of a foreign corporation to U.S. persons, especially subsequent to the repeal of Internal Revenue Code Section 958(b)(4) under the Tax Cuts and Jobs Act of 2017.[7]

For example, consider a situation in which a foreign person ("FP") owned all the stock in each of a domestic corporation ("Domestic Sub") and a foreign corporation ("Foreign Sub"). Section 318(a)(3)(C) would cause FP to attribute its shares of Foreign Sub to Domestic Sub, thereby making Foreign Sub a CFC of Domestic Sub. [8] The significance of the above discussed CFC attribution rules is they can be applied to attribute stock ownership of a Canadian company (and potentially other foreign entities) to the U.S. Subsidiary which holds U.S. real property. Thus, a U.S. corporate subsidiary could be considered as owning the stock of its foreign parent corporation and foreign corporations related to the foreign parent corporation directly or indirectly for U.S. tax and U.S. filing obligations.

HOLDING U.S. REAL ESTATE THROUGH AN LLC

Some Canadian real estate investors may consider placing U.S. real property in a limited liability company or ("LLC"). U.S. real estate investors often hold real estate in an LLC for asset protection and income tax reasons. These LLCs are typically disregarded for U.S. tax purposes. Although holding real property in an LLC that is disregarded for U.S. tax purposes may be beneficial to U.S. investors, such a structure will not likely be beneficial for Canadian real estate investors. Canadian investors holding U.S. real estate through an LLC taxed as a disregarded entity will be subject to the U.S. branch profits tax. An LLC treated as a disregarded entity for U.S. tax purposes does not qualify for a reduction of the 30 percent branch profits tax under the U.S.-Canada income tax treaty.

USE OF A LIMITED PARTNERSHIP TO HOLD U.S. REAL PROPERTY

Canadian real estate investors can hold U.S. real property through a limited partnership. A Canadian limited partnership can elect to be treated as a corporation or partnership for U.S. tax purposes. A partnership should be a Canadian partnership for Canadian income tax purposes if all the members of the partnership are Canadian residents. Canadian partners will need to file Canadian and U.S. income tax returns. The income tax returns would differ in terms of depreciation, whether interest may be deducted or capitalized, foreign exchange rules, and the utilization of losses. If the Canadian partnership is carrying on a trade or business, each general and limited partner is deemed to be carrying on a trade or business and is taxable in the United States on effectively connected income.[9]

The disadvantage of using a partnership to own the U.S. real property interest is that the partnership will be subject to Canadian income tax if it increases the property's mortgage above the property's original cost and distributes the excess mortgage proceeds to its partners. Another disadvantage is that Canadians who invest through a partnership will not benefit in Canada from the tax deferral available in the United States under the like-kind exchange in Section 1031 of the Internal Revenue Code. A limited partnership is also subject to the FIRPTA rules discussed above.[10]

INVESTMENT IN A U.S. REAL PROPERTY THROUGH A REIT

Finally, a Canadian investor may consider utilizing a real estate investment trust ("REIT") to hold U.S. rental investment property. In general, REITs have fully transferable interests and are widely held, having a minimum of 100 investors. REITs make current distributions out of income derived from U.S. real estate investments. The distributions are taxed in the United States as corporate distributions but there is no U.S. corporate-level tax. However, under Article VII(c) of the U.S.-Canada income tax treaty, the REIT must withhold U.S. tax at 5 percent on dividends paid by U.S. REIT: (1) to a Canadian resident individual owning 10 percent or less of the REIT; (2) if the dividends are paid regarding a class that is publicly traded and the beneficial owner is a person owning not more than 5 percent of any class of stocks; or (3) if the REIT is diversified, the owner owns 10 percent or less of the interest in the REIT. In all other cases, the U.S. withholding tax rate is 30 percent on dividends paid to Canadian investors.

Under FIRPTA, foreign investors are generally taxed on gain or loss upon disposition of U.S. real investments in the same manner as if the foreign investor were engaged in a trade or business within the United States and if such gain or loss were effectively connected with a trade or business. One of the exceptions to the applicability of FIRPTA frequently relied on by foreign investors is the sale of stock in a domestically controlled REIT. REITs typically issue shares that trade on stock exchanges and are bought and sold like stocks. To qualify as a REIT, a company must comply with certain provisions of the Internal Revenue Code. These requirements include to primarily own income-generating real estate for the long term and distribute income to shareholders. A REIT must also: 1) invest at least 75 percent of total assets in real estate, cash, or U.S. Treasuries; 2) derive at least 75 percent of gross income from rents, interest on mortgages that finance real property, or real estate sales; 3) pay a minimum of 90 percent of taxable income in the form of shareholder dividends each year; 4) be an entity that is taxable as a corporation; 5) be managed by a board of directors or trustees; 6) have at least 100 shareholders after its first year of existence; and 7) have no more than 50 percent of its shares held by five or fewer individuals.

CONCLUSION

The foregoing discussion is intended to provide the reader with a basic understanding of the principal alternatives and basic tax considerations of Canadian investment in U.S. real estate. It should be evident from this article, however, that this is a relatively complex subject. As a result, it is crucial that a Canadian real estate investor and his Canadian tax advisor review his or her particular circumstances with a qualified U.S. tax attorney when planning a proposed U.S. real estate investment.

End Notes

[1] *See* Treas. Reg. Section 1.897-1(d)(1).

[2] *See* Treas. Reg. Section 1.897-1(d)(2).

[3] *See* "Using Shared Appreciation Mortgages to Avoid FIRPTA," Florida Bar Journal, Vol. 80, No. 3 March 2006, Pg 40 Jeffrey Rubinger.

[4] Section 20(1)(c) of the Canadian Tax Code permits a deduction for interest if it relates to the purchase of an interest in U.S. rental property.

[5] Section 897(i) permits a foreign corporation having a permanent establishment in the United States that is protected by a nondiscrimination clause in a tax treaty to elect to be treated as a U.S. corporation for purposes of Section 897 and Section 1445 withholding requirements. The result of such an election is that the sale of real property by the electing foreign corporation would not trigger Section 897.

[6] For U.S. tax purposes, a CFC is a foreign corporation in which U.S. shareholders own more than 50% of the total combined voting power of all stock or the total value of the company's stock. *See* IRC Sections 957(a), 951(a), and 951(b).

[7] In the CFC context, Section 958(b) provides that the constructive ownership rules of Section 318(a), with certain modifications, apply for purposes of determining whether: 1) a U.S. person is a U.S. shareholder; 2) a foreign corporation is a CFC; 3) the stock of a U.S. corporation is owned by a U.S. shareholder; and 4) a corporation or other person is related to a CFC.

[8] *See* "The Modern Day Closely Held Foreign Corporation Post-Tax Reform," Steven Hadjilogiou and Fred Murray 2020).

[9] *See* "Canadian Investing in U.S. Real Property," Jack Bernstein (2016).

[10] Id.