

Breaking Developments in Tax Law

03/12/08

Withholding of Oregon Tax on Out-of-State Sellers of Oregon Real Estate

In the 2007 regular session, the Oregon Legislature adopted ORS 314.258, requiring any person that is an “authorized agent” to withhold and pay to the Oregon Department of Revenue (the “Department”) a portion of the consideration received in a “conveyance” of an Oregon “real property interest” when the transferor is an out-of-state individual or corporation (the “2007 Act”).

During the February 2008 special legislative session, the Legislature limited the broad scope of the withholding rule and corrected some technical problems (the “2008 Act”). Following are key points to be aware of:

What Sales Are Covered by the Withholding Rule?

“Conveyance” is defined as “a transfer or a contract to transfer fee title to any real estate located in the State of Oregon.”

Note: The 2007 Act’s all-encompassing definition of “real property interest” by reference to section 897(c) of the Internal Revenue Code of 1986, as amended (the “Code”), has been eliminated in favor of the usage of “real estate” in the definition of “conveyance.”

Withholding is required on a conveyance when the “transferor” is either:

- an individual who is not an Oregon resident; or
- a subchapter C corporation that is not domiciled, registered or otherwise qualified to do business in Oregon.

Who Must Withhold?

An “authorized agent” with respect to the conveyance must withhold and pay the funds to the Department. An authorized agent is either:

- a licensed escrow agent in a real estate closing escrow as governed by state statute;
or

- an attorney for a transferor or transferee who, simultaneously with the conveyance, deposits the unpaid purchase price into the attorney's client trust account for disbursement pursuant to the agreement between the parties.

An attorney who is an authorized agent is not required to withhold when a licensed escrow agent is providing services in the conveyance.

What Must Be Withheld?

The authorized agent must withhold and pay to the Department the least of the following three amounts:

- 4 percent of the consideration (including any encumbrance assumed by the transferee or to which the property remains subject);
- the net proceeds to be disbursed to the transferor, prior to reduction for withholding, as shown on the transferor's settlement statement; and
- 8 percent of the gain includible in the transferor's Oregon taxable income.

In arriving at this last amount, the authorized agent may rely on the transferor's written affirmation of the amount of includible gain.

Credit for the Amount Withheld

The transferor claims the amount withheld and paid by the authorized agent to the Department on the transferor's personal income tax return or corporate income or excise tax return.

Exception to Withholding in Certain Circumstances

An authorized agent is not required to withhold in connection with a conveyance if:

- the consideration is not more than \$100,000 or the amount to be withheld is less than \$100 (or another amount established by departmental rule);
- the conveyance is pursuant to a judicial foreclosure proceeding, a writ of execution, a nonjudicial foreclosure of a trust deed, or a nonjudicial forfeiture of a land sale contract;
- the conveyance is in lieu of foreclosure of a mortgage, trust deed or other security instrument, or a land sale contract with no additional monetary consideration;
- the transferor is a personal representative, executor, conservator, bankruptcy trustee, or other person acting under judicial review;
- the transferor delivers to the authorized agent written assurance as provided in section 6045(e) of the Code that the sale or exchange qualifies for exclusion as gain from the sale of a principal residence under section 121 of the Code; or
- the authorized agent obtains a written affirmation that the transferor is unlikely to owe Oregon income tax as a result of the conveyance.

Interest and Penalties

Penalties may be imposed on an authorized agent who does not comply with a withholding obligation. It is a defense to any claim by the Department or a transferor that the authorized agent acted in reasonable reliance upon representations made by the transferor or the transferor's tax advisor.

Effective Date

The 2008 Act applies to conveyances that occur after December 31, 2007. Compliance with the provisions of the 2007 Act before May 23, 2008, *i.e.*, the effective date of the 2008 Act, will be considered compliance with the 2008 Act.

Administrative Rules and Forms

OAR 150-314.258, adopted to implement the provisions of the 2007 Act, does not reflect the changes in the 2008 Act. The Department plans to adopt a temporary rule that will take effect on May 23 and expects to adopt a permanent rule by the end of August. In addition, a revised Form OR-18, to be used by an authorized agent to report withholding of tax under the 2008 Act, should be available on or before May 23.

For more information, please contact the Tax Law Practice Group at Lane Powell:

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