THE GUIDE TO FOREIGN INVESTMENT IN UNITED STATES REAL ESTATE

TIMOTHY D. RICHARDS

VAN NOSTRAND REINHOLD COMPANY
NEW YORK CINCINNATI TORONTO LONDON MELBOURNE

Library of Congress Catalog Card Number: 83-1151
ISBN: 0-442-27215-4

Manufactured in the United States of America

Published by Van Nostrand Reinhold Company Inc.
135 West 50th Street
New York, N.Y. 10020

Van Nostrand Reinhold Company Limited
Molly Millars Lane
Wokingham, Berkshire, England

Van Nostrand Reinhold
480 Latrobe Street
Melbourne, Victoria 3000, Australia

Macmillan of Canada
Division of Gage Publishing Limited
164 Commander Boulevard
Agincourt, Ontario M1S 3C7, Canada

15 14 13 12 11 10 9 8 7 6 5 4 3 2 1

Library of Congress Cataloging in Publication Data
Richards, Timothy D.
The guide to foreign investment in United States real estate.

Bibliography: p.
Includes index.
1. Real estate investment—United States.
2. Investments, Foreign—United States. 3. Real property—United States—Foreign ownership.
4. Investments, Foreign—Law and legislation—United States. I. Title.
HD1382.5.R5 1983 346.7304'3 83-1151
ISBN 0-442-27215-4 347.30643

Preface

The role of the foreign investor in the United States has been and will continue to be an important factor in the development of the United States' economy and culture. The counseling of the foreign investor is an exciting and challenging career for several reasons. Firstly, the foreign investor must formulate a plan to establish himself physically and economically in a new environment full of risks and opportunities. Secondly, the foreign investor is subject to a variety of laws and regulations which are constantly being amended and revised. New developments in these areas appear with such regularity that the foreign investor advisor must continuously update his knowledge.

This book has been prepared by experts and is intended for use as a reference. Due to the constant state of flux of the many areas, both legal and regulatory, which affect the foreign investor, professional guidance should always be sought. This book is not intended to be a substitute for the counsel of an attorney or other qualified professional.

As the world continues to grow smaller and as the global economy continues to expand, so will foreign investment in the United States. Professionals who advise foreign investors may actually be responsible in part for the internationalization of the U.S. economy.

TIMOTHY D. RICHARDS

Contents

Chapter 1
Introduction

OVERVIEW

The primary purpose of this book is to acquaint the U.S. investment advisor with the various problems and issues which foreign investors may face while investing in U.S. real estate. A secondary goal of this work is to educate the foreign investor who is contemplating an investment in the United States.

Chapter 2 will provide the reader with a general overview of the variety of real estate investments presently available in the United States. This chapter will briefly summarize the characteristics of agricultural, residential and commercial properties.

Chapters 3 and 4 will provide a detailed study of the many complex Federal and State reporting requirements to which a foreign investor or his advisor/intermediary may be subject. Such reporting requirements, especially those imposed on a state level, may be important factors in choosing the location of a foreigner's investment. Reporting requirements also affect the degree to which the foreign investor may retain his anonymity vis-à-vis his home jurisdiction.

Chapter 5 will address the problems of structuring the investment. This chapter will include suggestions for formulating an investment plan and assembling an investment team. It also includes a review of the mechanical aspects of the various ownership vehicles available to the investor together with some of their tax benefits. These vehicles will include foreign corporations, partnerships, joint ventures and trusts.

Chapter 6 will present a detailed discussion of the taxation of income and capital gains resulting from ownership of U.S. real estate, an area which has changed radically in recent years. The discussion is intended not only as basic text in the area but also as an update on the latest legislation. This chapter will also provide practical guidance and specific tax planning ideas.

Chapter 7 will provide an in-depth look at gift and estate taxation as it affects the foreign investor. Estate planning can be as important from the outset of an investment program as any other factor determining investment structures. Gift taxation may also be an important estate planning mechanism which the foreign investor may want to consider when formulating his overall plan.

Chapter 8 will provide a concise overview of the immigration laws and problems which will affect the investor. As a part of his overall plan, the foreign investor may be interested in becoming a citizen of the United States or a resident for tax purposes or immigration purposes. This chapter will explain the differences between visas available to the foreign investor.

Statistical Surveys of Foreign Investment in the U.S.

At a time when it appears that foreign investment in the United States has actually reached its heyday, and the tales of "exotic" foreign investors descending upon the United States have captured the imagination of the press and other media, it may come as a surprise to most that foreign investment in United States real estate is not a new phenomenon. According to a recent publication on the subject compiled by the New York State Bar Association, "The American colonies were creatures of foreign investment and at independence were still dependent upon foreign investment. After the revolution the new government was motivated to resolve outstanding British claims quickly and justly by the desire to assure credit worthiness in the eyes of European investors and thereby maintain a favorable climate for investment." Some of the nation's earliest leaders, such as Alexander Hamilton, argued for and upheld policies that encouraged foreign investment in the United States. The New York Bar publication goes on to state that: "Indeed, the Louisiana purchase in 1803 was funded with a loan of 11.25 million dollars from England, France and the Netherlands. And it is estimated that Europeans made two thirds of the new investment in railroads during the 1800s, the decade of the United States' railroads greatest expansion." (A Guide To Foreign Investment Under United States Law, American Bar Association, p. 2)

The trend in foreign investment continued on in the 1800s as European investors bought interests in short line railroads, canal projects, building projects and other businesses. This trend has continued until the present day. The spirit of this book is intended to encourage and promote the investment activity which has made the United States one of the greatest and most powerful nations in the world.

In the 20th Century political unrest in Latin America and Europe fueled another resurgence of foreign investment in the United States. This surge, combined with the ability of newspapers and other media to cover such trends, has made foreign investment in the U.S. a recurrent political issue. These political battles are fought mostly on the state level, as will be seen later. For the most part, federal activity in this area has amounted only to studies of foreign investment patterns and techniques.

The increase in foreign investments witnessed recently can be traced back to the generally depressed market of United States corporate securities in the early 1970s and the then declining value of the dollar on the international exchange markets. These two factors made United States securities and United States properties bargains for alien investors. A third factor may be that in the mid- and late 1960s the United States had developed massive balance of payments deficits resulting in excessive holdings of U.S. dollars abroad. OPEC activities, which caused a rise in the price of oil, contributed to the steady availability of dollars on the foreign market.

The dramatic increase in foreign investment gave rise to equally dramatic allegations of the horrors of foreigners taking over many U.S. businesses and huge tracts of agricultural land. The political thrust of these arguments was that foreign investment in the U.S. may be threatening the American way of life. In response to these attacks on foreign investment, the House of Representatives held hearings in January and February of 1974 on the subject of direct foreign investment in the United States. Testimony was received by the legislators; but the consensus following the hearings was that there was no statistical base upon which to formulate any appropriate legislation. In 1974 Congress directed the Commerce and Treasury Departments to conduct studies and compile statistics on the full range and extent of foreign investment in the United States. (Foreign Investment Study Act of 1974, P.L. 93–479, 88STAT.1450.) In 1976 Congress enacted the International Investment Survey Act to provide the President with the authority to investigate foreign investment and to divulge such information to the general public.

The first Commerce Department report reflects 1974 data, (Report to Congress by the Secretary of Commerce, "Foreign Direct Investment in the US, April, 1976, Volume 2.") The statistics encompass investments by U.S. affiliates of foreign investors, as well as direct investments by foreigners. The Commerce Department defined a U.S. affiliate of a foreign investor as a U.S. branch of a foreign corporation or a U.S. corporation in which at least 10% of the equity is owned by foreign investors. The data excludes affiliates having a net worth less than $100,000.00.

In 1974 foreign affiliates reported assets worth $4.2 billion, of which $2.6 billion was in property, plants, and equipment, with $621 million in property alone. Property, plant and equipment held by real estate affiliates increased by 20% between 1973 and 1974. The Commerce Department also estimated that foreign affiliates owned 1.1 million acres of U.S. agricultural land by the end of 1974.

The Commerce Department Office of Foreign Investment in the United States prepares annual tabulations of foreign purchases in U.S. real estate as reported in the press (Department of Commerce Press Release, June 13, 1979). In 1978, tabulations showed 158 transactions, 46 of which did not report a price. The average transaction value was a little higher than $10.3 million. Some 13 transactions had a value in excess of $25 million and these transactions accounted for 62% of the total investments identified.

An examination of the transactions reported to the Commerce Department in 1979 on a country basis illustrates a surprisingly small use of tax havens. However, many of the investors may have been obtaining tax shelter benefits in their home countries. Most of the large-scale investors were Canadians who were responsible for 35% of the total transactions and 51% of the value of the transactions. Investors from the Netherlands and investors using the Netherlands Antilles each represented 8% of the total number of transactions and 3% of the dollars invested. United Kingdom investors represented 6% of the transactions and 7% of the dollars invested. West Germans were involved in 9% of the transactions and supplied 7% of the monies invested. The Commerce Department data indicate a smaller percentage of investors using tax haven corporations than the Treasury Department data disclose.

Approximately 6% of the transactions were only identified, and no amounts were reported for these transactions. They were probably undertaken by foreigners who have various reasons for not disclosing their nationalities for fear of political repercussions, criminal sanctions or other personal reasons. As will be seen in Chapter 3, new reporting requirements that are imposed under the Foreign Investment In Real Property Tax Act may discourage investors who seek guaranteed anonymity when investing in this country. However, the general trend will probably not be affected significantly by these reporting requirements.

Statistics describing foreign investment in U.S. agricultural land are more current. The report issued in 1978 by the General Accounting Office (General Accounting Office Report on Foreign Investment, 1978) shows that foreigners own 0.3% of the land in the counties surveyed. If these counties are typical of the United States as a whole, foreigners owned 3 million acres of the one billion total acres of U.S. agricultural land in 1978. The 1974 Commerce Department estimates as of 1974 had indicated that foreigners owned 1 million acres, thus demonstrating a 200% increase between 1974 and 1978.

Available statistics do not indicate the average price per acre paid by foreign investors. Evidence suggests that foreigners tend to invest in higher quality agricultural land with a higher than average price. The Department of Agriculture estimates that foreign-owned land is worth about $1,000 dollars per/acre as compared with the U.S. national average of $561. Several senators have expressed fears that foreigners are inflating the price of agricultural land, (speech by Senator Wallop, June 27, 1979). These legislators believed that the foreigners could pay more because they were exempt from paying capital gains tax when the land was resold, and that the overall impact of imposing a capital gains tax on nonresident aliens would reduce or stabilize the price of agricultural land in the long run. This conclusion is speculative and may be mere political rhetoric, in that it ignores the fact that foreigners investing in the United States are more concerned about investment security and therefore prefer higher quality assets.

According to Department of Agriculture estimates, the amount of agricultural land bought by foreigners in 1977 and the first half of 1978 averaged 560,000 acres per year, or 2% of the acres sold during that period. The value was $560 million, or 4% of the total value of agricultural land sold in 1977.

Politicans in the Midwest and other farming areas have created two myths:

1. Foreign investment in U.S. agricultural land will change present land ownership patterns by excluding small-time farmers.
2. Foreign investors will remove their agricultural land from production, thereby causing a decrease in the U.S. food supply.

As will be seen in Chapter 4, various states have attempted to enact laws which may control the foreign investor's ability to purchase and hold U.S. agricultural land. The fact that this xenophobia exists is good cause for the exercise of discretion on the part of any foreign investor who desires to purchase U.S. agricultural land.

The Agriculture Foreign Investment Disclosure Act of 1978 requires all foreigners to inform the government if they own agricultural land in this country. This information is public, and a recent Agriculture Department study based on the statistics gathered shows that foreigners own 5.2 million acres of the nation's 1.2 billion acres of farmland and ranchland. Europeans, not Arabs, have been doing most of the buying in recent years. Investors from the United Kingdom, Luxembourg and West Germany hold 52% of all foreign-owned farmland. These statistics show that U.S. corporations with at least 5% foreign ownership own 76% of "foreign-held" agricultural land.

This study concluded that the amount of land owned by foreigners is so small that it is unlikely to have a significant effect on prices. A 14% increase in farmland prices in 1980 was not statistically related to the relative increase in foreign investment. The final conclusion of the study states that foreigners tend to increase production on the land in which they do invest.

The average size of the foreign purchase of arable land was 1,141 acres, almost 4 times as large as the U.S. average of 308 acres. The average foreign purchase was worth about $1.1 million and was about 6 to 7 times larger than the average domestic purchase. These differences may not be as dramatic as the data indicate because most foreigners are making first time purchases, which are normally larger than supplemental purchases. Domestic buyers are usually making marginal additions to their present holdings. Therefore, first time domestic purchasers are the most affected by the pattern of foreign investment in agricultural land. It is doubtful, however, that the capital gains tax imposed on foreigners will alter this pattern enough to favor the first time domestic purchaser. Actually, the new tax law may discourage foreigners from selling their holdings, thereby actually tightening the supply of agricultural land and raising the cost of first time domestic purchases.

The most recent statistics compiled under the authority of the Agriculture Foreign Investment Disclosure Act of 1978 are reported as follows in a recent periodical:

> In April the United States Department of Agriculture released to Congress its annual AFIDA Report. The report shows that foreigners own 12.7 million acres of U.S. agricultural land as of December 31, 1981, which is slightly less than 1% of all privately held agricultural land and 0.6% of all land in the U.S. The report revealed that foreign persons from Canada, France, United Kingdom, Germany, and the Netherlands Antilles account for 78% of the foreign held acreage. Except for Maine, foreign holdings are concentrated in the South and Southwest. According to the report, foreigners do not appear to be taking purchased agricultural land out of production. In general the quantity of foreign owned U.S. agricultural land is too small to measure the impact of agriculture on a national level. (Bruce Zagaris, 30 *Taxes International,* April 1982, page 12.)

Therefore it appears that although foreign investment in agricultural land is measurable, its impact on the overall economy of the U.S. is probably negligible.

Tax return statistics compiled by the Treasury Department for 1974 and 1975 indicate that the ownership vehicle favored by most domestic and foreign investors in real estate was the partnership format. Real estate owned through a partnership accounted for 49% of the total receipts from the real estate business. Real estate investors may have preferred partnership forms because losses flow through to the partners and may shelter the U.S. partners' other income from taxation. (IRC Section 731(b)).

The total receipts of foreigners in foreign-controlled domestic corporations holding U.S. real estate comprised about 3% of the total receipts of all U.S. real estate corporations and 1% of the total receipts of all U.S. corporations and partnerships. These percentages do not include the rental income of foreign individuals, trusts and estates owning U.S. real estate in their own names or holding interests in a U.S. real estate partnership.

According to IRS data, foreign owners of domestic corporations most often listed addresses in Canada (34%) and in the Caribbean (20%). In contrast, 43% of the foreign corporations owning U.S. real estate, representing 60% of the gross receipts, reported an address in the Caribbean. Only 23% of the foreign corporations, representing 22% of the gross receipts, reported addresses in Canada. Foreign corporations incorporated in the Caribbean can often issue bearer shares and assure the anonymity of their beneficial owners. This concern for anonymity is reflected in statistics which indicate that 12% of the foreign-controlled domestic corporations declined to report any foreign address.

Prior to the enactment of FIRPTA in 1980, foreign corporations domiciled in either Canada or the Netherlands Antilles could annually elect to be treated as having effectively connected taxable income. Tax treaty provisions currently in effect enable this election to be revoked in the year a sale is made. Gain from that sale was then exempt from capital gains tax under U.S. statutory law.

Treasury Department data show that foreign investment in U.S. real estate through U.S. corporations is much larger than direct ownership by foreign corporations. A U.S. corporation cannot escape the capital gains tax on sales of real estate. It appears that the capital gains tax consequences of foreigners investing in U.S. real estate is only the tip of the iceberg of incentives which cause foreigners to pour their wealth into the United States.

A recent study done by the public relations firm of Hill and Knowlton concludes the following:

> By the most conservative estimate, the amount of foreign direct investment in the United States doubled from 1974 to 1978 and will probably continue on a steadily upward path through the 1980s. While significant foreign presence is not new to the U.S., the rapidity with which foreign companies have jumped on the investment band wagon and the fact that many new investors are of a nationality considered "exotic" by certain sectors of the American public have drawn the foreign investor more and more into the public eye and have subjected the companies to public and political pressures. The pressures are escalating at the end of the '70s. While it might not have been the case in the past, the American consumer now is aware that many of his favorite products are imported from foreign countries or are produced in the United States by foreign-owned firms. More importantly for the investor, however, that awareness has led in some instances to the foreign company being made the target of criticism for deep-seated American economic problems. The most dramatic example of the phenomenon occurred recently when protests against the lines at gas stations in some parts of the U.S. were directed at Shell Oil, not only for being an oil company, but for being a foreign-owned one. This new visibility could snowball as the U.S. experiences a period of economic readjustment in the 1980s. [*Hill and Knowlton Survey,* 1980, p. 2.]

Despite the high publicity profile of foreign-owned companies and foreign investments, there is no indication that foreign investors will cease to have a great interest in the United States as a potential investment market. The real attraction of the United States investment market will continue to exist. There is no single answer to the question of why foreigners choose to invest in the United States. However, there is no doubt that the rapid growth of foreign investment is enhanced by the relative attractiveness of the United States as a market when compared with all other potential investment areas. A foreign entity seeking to invest in the United States can look forward to decent market growth, nominal governmental interference, long-term investment security and relatively few labor problems. There is no doubt that the free market of the United States enables competitively oriented corporations and investors to operate freely and productively as compared to the socialized and highly regulated societies of Western Europe, Latin America and Asia where government regulations have become too burdensome and political risks too numerous.

The popularity of the U.S. market is undoubtedly related to its great size and diversification. This size, combined with a democratic form of government wherein the mini-revolutions of the republic are fought by ballot instead of by bullet, constitute major attractions for foreign investors.

Additional factors of significant importance are: the ample availability of labor, management, and financing skills; excellent marketing and distribution systems for products made possible by efficient telecommunication and public transportation systems. These factors, coupled with the high development of technology and great natural resources, make investing and supervising an investment in the United States attractive. The Hill and Knowlton study continues:

> Since these same attractions might have been enumerated during the 1960s or even the 1950s, it is necessary to go beyond them to find out why foreign companies have increased their investment activities recently. Other economic events are behind this phenomenon—the freeing of the U.S. dollar from the gold standard and the dollar's subsequent decline, supplemented by the OPEC oil embargo of 1973. Dollar based assets never looked so good to European investors who were suffering from increasingly hard currencies. Long term profitability suddenly required that a large European or Japanese multinational have a U.S. presence. The OPEC oil price rises generated the transfer of wealth to that area, but much of it was recycled back into the U.S. through the intermediary of European banks. Coupled with these economic changes, political socialization trends in Europe gave the U.S. a comparatively rosy glow as the "last bastion of free enterprise" and the final battleground for the true entrepreneur. [*Hill and Knowlton Survey,* 1980, page 3.]

There is no doubt that the influx of larger investors and multinationals attracted the attention of medium-size and small investors in both European and Latin American markets. Even the small investor with only tens of thousands of dollars to invest has become enthralled with the idea of investing in the United States. This investor, although not large enough to influence the statistics cited above, is nonetheless interesting from a business standpoint.

Attorneys, real estate brokers, and investment advisors who become professionally associated with the smaller investors are often impressed by the extent of the individual wealth held by families. The American way of life does not foster or necessarily encourage the family business, a family fortune, or the family enterprise. However, the cultures of Europe, Latin America, and the Middle East tend to encourage family involvement in business. Latin

American and European investors often possess extensive family ties and extremely strong political connections in all areas of their home governments. Such families may have reputations that extend back for generations.

CONCLUSION

The statistics compiled by the Department of Commerce, the Treasury Department and the Department of Agriculture are incomplete. These statistical surveys are generalized, and purport to reflect only large investments. Totally left out of the picture is the smaller and medium-size investor. The economic motives compelling these investors are essentially the same as those which compel larger investors. There are, however, often several other motives behind this special type of investor; in particular, peer pressure, fashion, and fear. With the world subject to unprecedented political and economic fluctuations, the small and medium-size foreign investor is naturally drawn to the United States through personal contacts with other foreign investors. Any investment advisor, banker, attorney, or accountant who deals regularly with this type of investor learns very quickly that the foreign client is often an avenue to a wide range of contacts. This network of foreign investors becomes an important source of information and camaraderie for other potential foreign investors.

The smaller investor usually comes to this country through one of the larger, well known cities such as Miami, New York, New Orleans or San Francisco, and must be introduced to and ushered through the various procedures, regulations and formalities of the American business world. The U.S. professional investment advisor, attorney, real estate broker or accountant must be prepared to educate the foreigner and service his special needs. It is usually true that once the foreigner has been properly educated and has made several sound or successful investments, his friends and associates from abroad get the positive feedback and encouragement they need to make the decision to invest in the United States. The U.S. national who advises the foreigner bears a tremendous responsibility in this respect. He must take on the role of ambassador, educator and advisor. Foreign investors often insist on having a personal relationship with the investment advisor as well. Building this relationship, and becoming acquainted with the many different problems the foreigner will face, are challenges that U.S. advisors must take seriously.

Chapter 2
U.S. Real Estate

U.S. real estate is considered by both native and foreign investors to be an excellent long term investment. For many reasons the United States still has a plentiful supply of favorable real estate investments. While the foreign investor may face shortages of both capital and real estate at home, this is not the case in the United States. Moreover, the tax advantages and appreciation potential of U.S. real estate, considered along with the traditional status of real estate as a secure investment, make U.S. real estate almost irresistible to the foreign investor. The U.S. market is an active one and therefore real estate investments are relatively liquid when compared to similar investments in places where financing is not readily available.

U.S. investors often take many aspects of the U.S. real estate market for granted. This is particularly true in the area of finance. In many foreign jurisdictions investors are not able to finance purchases in the same manner as they can in the United States. Interest rates are often much higher than those found in the United States. Loans, when available, must often be personally guaranteed by the borrower. The following example illustrates the attractive features of the financing available in the United States:

> One of the benefits of such financing is the resulting increase in the borrower's purchasing power, commonly referred to as "leveraging" in the U.S. and "gearing" in many English jurisdictions. Consider, for example, the foreign investor who has $200,000.00 to invest. Assume that he has located a piece of U.S. real estate which can be purchased for $200,000.00 and which will generate a "cash flow" of $20,000.00 per year. If the foreign investor uses all of his cash to acquire the property, he will thus realize a cash return of 10% per annum, in addition to whatever appreciation potential is realized upon his ultimate disposition of the property.
>
> Assume, however, that the foreign investor can arrange long term financing in an amount equal to 80% of the purchase price, which is $160,000.00. Assume further that such financing requires annual payments of principal and interest in the amount of $16,000.00 per year, or 10% per annum of the original loan balance, which percentage is commonly referred to as the "loan constant."
>
> In this case, the foreign investor will have to advance only $40,000.00 to acquire the property, the difference between the $200,000.00 purchase price and $160,000.00 loan, but he will also enjoy the full appreciation potential

> that would have required a \$200,000.00 cash investment absent the financing. Cash flow after debts [is] dropped from \$20,000.00 per year to \$4,000.00 per year, and this will still represent a cash return of 10% per annum on the reduced cash investment of \$40,000.00. Alternatively, assuming the availability of five such properties, with the original \$200,000.00 cash investment the foreign investor will achieve the original \$20,000.00 per year cash flow while increasing his appreciation potential by 500% and diversifying or spreading the risk of his investment over five properties rather than just one property. [Ronald Barak, *Foreign Investment in U.S. Real Estate*, 1981, page 18.]

This chapter will provide a brief introduction to the variety of real estate investments available to the foreign investor.

ARGICULTURAL LAND

Agricultural land is still plentiful in the United States and is available in a variety of price ranges. The foreign investor may develop agricultural land or he may hold it for investment purposes while leasing the land to local farmers. Often the appreciation of such an investment is augmented when the agricultural land is located in the vicinity of newly developing residential and urban areas. Such properties are particularly attractive in the newly developing Southern states. In such cases "zoning," i.e., land use restrictions prescribed by the local government, will affect the value of any agricultural land near an urban or residential area.

Notwithstanding Federal and State reporting requirements imposed upon the foreign owner of U.S. agricultural land, foreigners can be reassured that their investment is secure.

Foreigners desiring to continue farming their U.S. agricultural land will find that resources in the United States available to the farmer are vast. Such resources include highly specialized technology, government support for agricultural production, and the steady supply of skilled agricultural technicians.

COMMERCIAL PROPERTIES

Shopping Centers

Shopping Centers are an excellent investment for the foreign investor because of the favorable financing available for such purchases, and, also because of the high cash flow that such investments are capable of producing. A major reason for the favorable cash flow associated with shopping centers is the leasing arrangements made with tenants. Tenants often pay a fixed percentage of their gross revenues in addition to a fixed rental amount per month. A landlord may require the installation of his own cash register system in each tenant's store so as to facilitate his auditing of each tenant's gross revenues.

The purchase of any shopping center requires careful evaluation and extensive legal analysis of each tenant's lease. The subsequent management of the investment is time consuming and may require the attention of a small staff of professional property managers. This administrative factor may require the close attention of the foreign investor on a monthly basis.

Office Buildings

Office buildings are available in all sizes, and are also considered to be popular investments for the foreign investor. The cash flow and appreciation in value of such investments are both positive factors. Lease arrangements can often be made with the tenant wherein the tenant is responsible for most maintenance charges associated with the upkeep of the building. These charges are revised on a yearly basis to reflect any increase in costs. Such yearly increases in rent are imposed on all tenants regardless of the length of their lease. Thus, the foreign investor can insure a positive cash flow.

The appreciation of office buildings is particularly high in urban areas undergoing rapid development. A city which is experiencing an increase in the size of its urban center will be able to support large increases in office space in relatively short periods.

RESIDENTIAL

Condominiums, Cooperatives, and Apartments

Foreign investment in U.S. condominiums, cooperatives and apartment buildings has increased dramatically over the past few years. These units are often the first investment a foreigner makes in the United States. Such units require very little maintenance and can be rented to tenants when not in use by the foreigner.

During the recent real estate boom in Miami, Florida several foreign investors purchased options on luxury residential units and later sold these options at a profit to other foreign investors. These options were attractive to the foreign investor because the developer's purchase price was lower than the market value for the equivalent unit. This type of investment is, at best, risky. During the ensuing real estate slowdown many investors in the Miami area who had intended to "flip" their contracts were faced with the prospect of actually having to purchase the unit or lose their deposit.

U.S. residential real estate, whether a condominium or a single family dwelling, has traditionally shown healthy appreciation. The location of these investments may have a great deal to do with future appreciation. Residential units which are near public transportation, good public schools, pleasant residential neighborhoods and other local attractions will steadily increase in value over the years.

Chapter 3
Federal Reporting Requirements

One of the greatest problems which the foreign investor must face is the disclosure required by Federal and State Governments. There are a myriad of reporting requirements with which foreign persons and entities must comply in order to avoid heavy fines and other penalties. The foreigner's U.S. agent, attorney, broker or accountant may be surprised to learn that he may be responsible for the foreigner's noncompliance and thereby subject to the same penalties.

Most of the reporting requirements have arisen only in the last few years. The authorities are aware that most people who should comply have not done so and may not even be aware of the requirements. The time will come shortly when the Federal Government will begin to seriously enforce the various reporting laws.

The anonymity which foreigners hope to find in the United States is threatened by these numerous disclosure statutes and regulations. Foreigners often face legal problems if the extent of their foreign investment is detected in their home jurisdiction. With proper care and planning of the investment structure, the U.S. disclosure requirements can be fully complied with and anonymity can, at the same time, be safely preserved.

REPORTING TO THE COMMERCE DEPARTMENT

The International Investment Survey Act of 1976 was passed by Congress in response to what was perceived to be an "invasion" of foreign investment. The Act was motivated by certain xenophobic elements in Congress who feared that America would be literally bought out by the "Oil Sheiks." The movement was joined by less radical Congressmen who felt the need to study the foreign investment phenomenon more closely. Without a solid statistical background, meaningful discussions on the subject were impossible.

Originally, the Act was not intended to provide a company-by-company report on foreign investments. It was meant only to provide raw data to policy makers in the form of aggregate investment statistics. The scope of authority contained in the Act is quite broad. The Act effectively provided in Section 5 that rules or regulations issued pursuant to the Act "...may require any person subject to the jurisdiction of the United States to furnish, under oath, any report containing information which is determined to be necessary to carry out the international investment surveys and studies conducted under this Chapter" (22 U.S.C. 33104(b)).

Regulations were then formulated by the Department of Commerce's

Bureau of Economic Analysis (BEA). The BEA published final regulations requiring reporting of all direct foreign investment in U.S. real estate, other than property held for personal use, on June 6, 1979 (42 Fed. Reg. 32, 586 (1979)). The required forms are numerous and require the disclosure of a great deal of financial information.

The final regulations promulgated by the BEA provide for two distinct categories of reports:

1. Transactional reports
   (a) Form BE13-A
   (b) Form BE13-B
   (c) Form BE13 supplement C
   (d) Form BE14
   (e) Form BE607
2. Periodic reports
   (a) Form BE-15
   (b) Form BE-12
   (c) Form BE-12 supplement C
   (d) Form BE605
   (e) Form BE606B.

In general, the Act requires one or more of the above forms to be filed by, or on behalf of, a foreign person whenever such person has acquired, directly or indirectly, a 10% or greater interest in a U.S. "business enterprise" (22 U.S.C. 33102(7)). A "business enterprise" is defined as "any venture which exists for profit-making purposes or to otherwise secure economic advantage, and any ownership of real estate" (22 U.S.C. 33102(6)). Under current interpretation the Act does not require filing by, or on behalf of, a foreign investor who merely has a security interest in U.S. real estate. Moreover, there are specific provisions which exempt a foreign investor who invests in a U.S. limited partnership because " . . .limited partners do not have voting rights in a partnership and therefore cannot have a direct investment in a partnership; their investment is considered to be portfolio investment" (15 CFR Section 806.12).

Another important exemption found in the regulations is: "Real estate held exclusively for personal use and not for profit-making purposes is exempted from being reported. A residence which is leased by an owner who intends to reoccupy it is considered real estate held for personal use" (15 CFR Section 806.8). Thus, a U.S. residence owned by a foreign person may be rented from time to time and the exemption will still be valid as long as the owner intends to reoccupy the premises. Apparently this exemption applies only to individual owners and not to corporations or other business entities holding real estate.

BE-13 Forms

A foreign investor who invests in any U.S. business enterprise on or after January 1, 1979 must complete one of the BE-13 series forms. Investments made before that date are exempt from being reported on the series of transactional reports. If a foreigner invests in less than 200 acres of U.S. real estate,